

CA26N

XC2

- 65-05417



ONTARIO

LEGISLATIVE ASSEMBLY

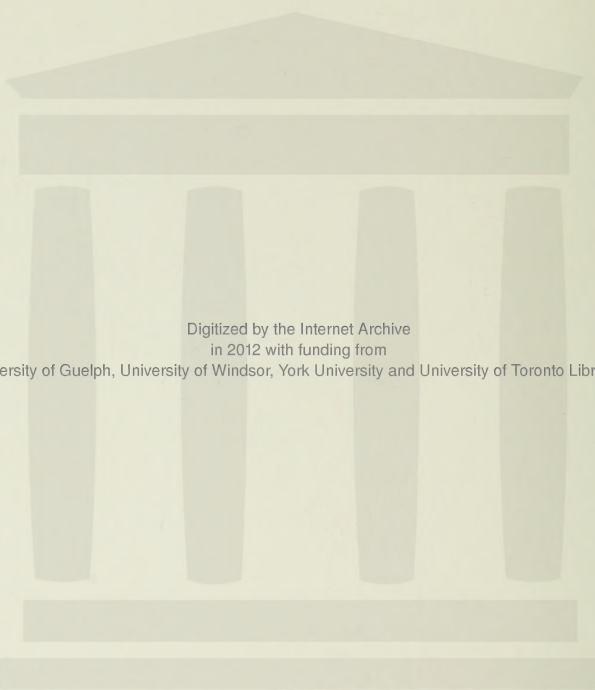
1978

THE INSURANCE INDUSTRY
SECOND REPORT ON
AUTOMOBILE INSURANCE

THE SELECT COMMITTEE
ON
COMPANY LAW

Tabled in the Legislative Assembly
by
JAMES R. BREITHAUP, Q.C., M.P.P.
CHAIRMAN

Second Session, 31st Parliament, 26 ELIZABETH II



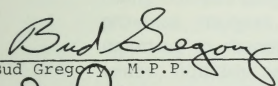
Digitized by the Internet Archive
in 2012 with funding from
University of Guelph, University of Windsor, York University and University of Toronto Libraries

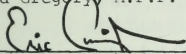
LETTER OF SUBMISSION

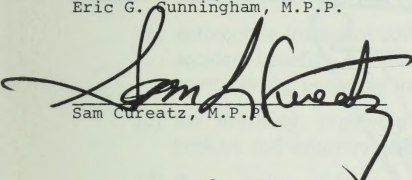
TO: The Honourable John E. Stokes,
Speaker of the Legislative Assembly of the
Province of Ontario

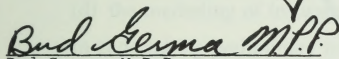
Sir:

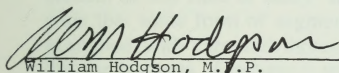
We, the undersigned members of the Committee appointed by the Legislative Assembly of the Province of Ontario on July 12, 1977, to enquire into and review the law relating to the business of insurance companies in the province, have now the honour to submit the attached Second Report on automobile insurance.

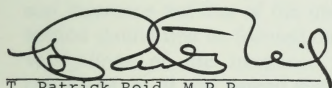

Bud Gregory, M.P.P.

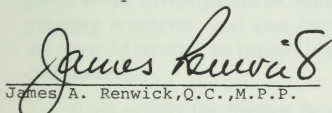

Eric G. Cunningham, M.P.P.

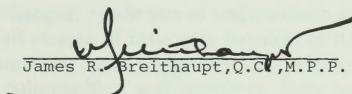

Sam Cureatz, M.P.P.

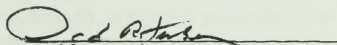

Bud Germa, M.P.P.

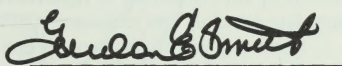

William Hodgson, M.P.P.

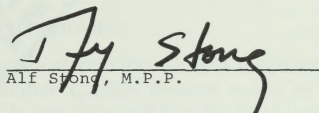

T. Patrick Reid, M.P.P.
Rainy River

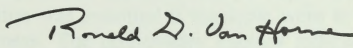

James A. Renwick, Q.C., M.P.P.

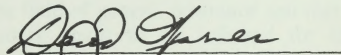

James R. Breithaupt, Q.C., M.P.P.

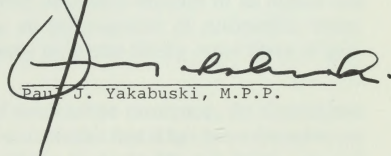

David Rotenberg, M.P.P.

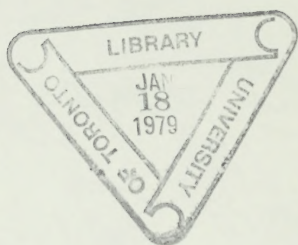

Gordon E. Smith, M.P.P.
Simcoe East


Alf Stone, M.P.P.


Ronald G. Van Horne, M.R.P.


David Warner, M.P.P.


Paul J. Yakabuski, M.P.P.



PREFACE

The Select Committee on Company Law was reconstituted on May 25, 1976 under the following terms of reference:

“to continue the enquiry and review of the law affecting the Corporations in this province as reported on by the Select Committee of this House appointed on June 22, 1965 and re-appointed on July 8, 1966, on July 23, 1968 and December 17, 1971 and to, in particular, enquire into and review the law relating to the business of insurance companies in the province including, but not restricted to,

- (a) the incorporation, licensing, regulation and supervision of insurers as joint stock companies, mutual corporations, fraternal societies, mutual benefit societies, exchanges, syndicates of underwriters and rating bureaus carrying on all classes of insurance business in this province, mergers, amalgamations and reinsurance of liabilities, reporting to shareholders, policyholders and members, their solvency, liquidity and financial requirements, the purposes, scope and functions of their returns, reports, statistical gathering, and the basis for their rates and premiums;
- (b) automobile insurance contracts and, in particular, the provision of accident benefits, fire insurance, accident and sickness and marine contracts and generally insurance contracts in this province;
- (c) the licensing, regulation and supervision of insurance agents, brokers and adjusters; and
- (d) the marketing of insurance in this province.”

In undertaking preliminary investigations into the business of insurance companies in the Province, the Committee quickly became aware of the breadth of this field of study. Indeed, it was apparent that the field was so wide that some form of segmentation was essential if the topic were to be examined with care and thoroughness. The preliminary enquiry indicated that the business of insurance was readily divisible into the business of general insurance and that of life insurance. It was decided, therefore, that attention should first be focused on the field of general insurance and that investigations of life insurance matters ought to be deferred for later consideration. It was agreed that priority within the non-life field should be given to the investigation of automobile insurance because of its urgent and pressing problems, and also because an investigation of automobile insurance would provide an insight into many problems facing other types of general insurance.

Even within the limited field of automobile insurance, the Committee has found such a variety of problems to consider that it has been forced to set certain priorities in the choice of problems to deal with and in the order of

their consideration. Accordingly, the Committee chose to issue two Reports on the topic of automobile insurance, the first dealing with some of the most pressing problems in the field and the second considering further the many substantial issues in the automobile insurance system. The Committee's First Report was submitted to the Legislative Assembly on March 28, 1977 by the Chairman, Mr. Vernon M. Singer, Q.C. The conclusions and recommendations set out in the First Report are appended to this Report as Appendix A.

In its First Report, the Committee announced its intention to deal thoroughly with a number of further matters in its Second Report. The topics outlined for subsequent consideration are presented in the Introduction to this Report.

On July 12, 1977, the Committee was reconstituted to conduct further enquiry and resumed its hearings with the appointment of thirteen members, as follows: Mr. Breithaupt (Chairman), Messrs. Cunningham, Cureatz, Germa, Gregory, Grossman, Laughren, McCaffrey, Reid, Renwick, Rotenberg, Stong, Van Horne and Yakabuski. Messrs. Laughren and McCaffrey and The Honourable L. Grossman resigned and, by order of the House, Messrs. Warner, Hodgson and Smith were appointed on December 15, 1977 to fill the respective vacancies that had been created.

Since its most recent reconstitution, the Committee has held sessions on 49 days. There have been over 80 witnesses before the Committee including some 40 persons with whom the Committee conferred during its sessions outside the Province. A list of witnesses is set out in Appendix B and the Committee wishes to thank them all for their assistance and to express its indebtedness to all those who contributed to the over 100 exhibits, submissions, briefs and other documents received by the Committee.

The Committee wishes to extend its gratitude particularly to those persons who came to Toronto to appear before the Committee to discuss the problems of automobile insurance that had arisen in their respective jurisdictions and the solutions that they have developed. The Committee is grateful to Messrs. Howard Baizaire, Administrative Assistant, Automobile Club of Michigan Insurance Group, and Jack Siebold, General Counsel and Director of Governmental Affairs for the Independent Insurance Agents of Michigan, for providing insight into the automobile insurance system in the state of Michigan. The Committee also thanks Messrs. Peter Ingham, General Counsel, and Michael Miller, Actuary, of the State Farm Insurance Companies for their assistance in explaining the background for automobile insurance regulation in the United States. In addition, the Committee is grateful to Mr. Jean Gregoire, Chairman of the Board of Directors, Insurance Brokers Association of Quebec, for his part in contributing to the Committee's understanding of recent developments in the field of automobile insurance in the Province of Quebec.

In September and early October 1977, the Committee travelled to Regina and Vancouver where it conferred with representatives of the government insurance corporations in Saskatchewan and British Columbia and met with other interested parties including representatives of the insurance industry in those Provinces. The Committee was pleased to meet with Mr. John Green, Q.C., General Manager of the Saskatchewan Government Insurance Office and the late Mr. Norman Bortnick, the former Vice-President and General Manager of the Insurance Corporation of British Columbia. Both gentlemen were intimately involved in the shaping of the government insurance systems in their respective Provinces. The Committee particularly wishes to express its appreciation to the Honourable Dr. P. L. McGeer, Minister responsible for I.C.B.C., for appearing before the Committee. The Committee concluded its investigations in the autumn of 1977 by meeting with officials of the California Insurance Commissioner's Office and industry representatives in that state to discuss aspects of the automobile insurance industry in a regulatory environment that has been likened to that of Ontario.

In January 1978 the Committee had the benefit of conferring with representatives from the government, the business and academic community and consumer interest groups in Boston, Massachusetts, Washington, D.C., and Miami, Florida. In Boston the Committee was fortunate to be able to attend a hearing on rate regulation of the Massachusetts Joint Committee on Insurance and to meet with Senator D. J. Foley, Co-Chairman of that Committee. In Washington, the Committee met with a number of federal government officials and representatives of the Senate Committee on Commerce, Science and Transportation and of the Joint Committee on Banking, Housing and Urban Affairs. In its sessions in Florida, the Committee was able to benefit from the views and investigations of a wide spectrum of interested parties representing the concerns of consumers, regulators and suppliers of automobile insurance. The range of interests represented by these witnesses provided the Committee with a most useful understanding of the problems in the automobile insurance field as perceived in other jurisdictions.

In addition to those who appeared before the Committee, our business consultants, Woods, Gordon & Co., interviewed a great many persons over the entire course of the Committee's investigations into automobile insurance. Representatives of the Superintendent's Office, the Insurance Bureau of Canada, the Insurers Advisory Organization, the Facility, the Independent Insurance Agents and Brokers of Ontario, individual insurance companies, adjusters, appraisers, other government departments and special interest groups concerned about the automobile insurance system in Ontario were contacted, all of whom were most co-operative in assisting with the research work. Other valuable contacts included officials of the government insurance corporations in Western Canada, the Provincial Auditors of Saskatchewan and Manitoba, officials of regulatory boards in selected Prov-

inces and representatives of state insurance departments and industry associations in the United States.

From the start of its investigations, the Committee was particularly eager to benefit from contributions and comments from members of the public of all backgrounds, not limited to those with expertise within the insurance industry. Accordingly, advertisements were placed in the press and invitations were extended to members of the public to appear, to submit briefs, and generally to assist the Committee. In order to encourage further contributions from the public at large, the Committee conducted, prior to issuing its First Report, special sessions during October 1976 in London, Ottawa, Sudbury and Toronto. The advertisements and special sessions resulted in the presentation of numerous briefs and submissions by the public whose contributions served to guide the Committee's deliberations throughout its entire investigations.

The Office of the Superintendent of Insurance of Ontario has given generously of the time of its staff and they have made a major contribution in assisting the Committee. Mr. Murray A. Thompson, Q.C., Superintendent of Insurance of Ontario, has been of special help, as have Mr. Lear P. Wood, Director of Insurance Services, Mr. Marshall P. Dawson, Co-ordinator of Automobile and Casualty Insurance; Mr. Ernest H. Miles, the Director of the Motor Vehicle Accident Claims Fund; and Mr. Brian Newton.

The Committee is very much indebted to our Consultants, Woods, Gordon & Co., who did research and reported to the Committee by way of thirteen Reports, five corresponding to the Committee's First Report and eight corresponding to the Second Report. Reports Nos. VI, VII, VIII, IX, X, XI, XII and XIII will be placed in the Legislative Library along with a copy of this Report and the previous Reports of the Committee and its consultants. Mr. R. Paul Boddy, C.A., Mr. P. D. McKelvey, C.A., and Miss L. Jagielicz, M.B.A., representatives of Woods, Gordon & Co., have attended all meetings and assisted in the writing of this Report; their assistance and guidance have been invaluable.

The Committee would like once again to express its sincere appreciation to our Counsel, Mr. R. George Ness, Q.C., of the firm of Ness & Winters, for his guidance during our meetings and for his part in the writing of this Report. His ability and his continued attention to the tasks of the Committee have contributed greatly to both the First and Second Reports.

The Committee's very special gratitude goes to Mrs. Frances Nokes, who has been the Clerk of the Select Committee since it was first created. Her loyalty and her ceaseless efforts have, as ever, been invaluable to the Committee.

Our gratitude is also due to Mrs. Dorothy Gibbs and Mrs. Frances Davidson of the Clerk's Office, and Mrs. Irene Boyko of Woods, Gordon &

Co., who helped so ably with the myriad details and with the typing involved in publication of this Report.

It is the Committee's intention to continue its studies and to submit subsequent Reports on other aspects of the business of general insurance and of life insurance.

INTRODUCTION

The automobile insurance system and the automobile insurance product have evolved from "socially" acceptable principles of loss distribution, rate determination and entitlement to compensation dating back in many instances half a century. According to its terms of reference, the Select Committee on Company Law undertook to study in some detail the present system of automobile insurance and the operations of the insurance companies in the Province. It became apparent to the Committee in its investigations that the time had come for a fundamental re-examination of the automobile insurance system in the light of the present-day protection and coverage needs of the Ontario resident and motorist.

However, as indicated in the Preface, the Committee recognized early on that an exhaustive study of the automobile insurance system would be impossible without considerable time and resources. Accordingly, it chose to deal with what were felt to be the most pressing problems in the First Report and to defer further topics or matters on which the Committee required additional information to a Second Report.

In its recommendations in the First Report, which are set out in Appendix A, the Committee considered two matters to be of major significance. Firstly, the Committee recommended that every person who owns a licenced automobile be required to have a valid policy of automobile insurance providing third-party liability coverage and Accident Benefits coverage. Secondly, the Committee proposed improvements in the present Accident Benefits coverage. Subsequent to the issuance of the First Report, the government announced its intention to move towards implementation of compulsory automobile insurance, and also announced new regulations with respect to Schedule E of the Insurance Act. Schedule E prescribes Accident Benefits which are mandatory whenever a third-party liability policy is issued. The new scale of benefits in general follows the recommendations of the Committee as set out in the First Report.

In concluding its First Report the Committee outlined topics deferred for subsequent consideration; these were as follows:

1. Investigation of Various "No-Fault" Systems

The Committee will review the current status of no-fault plans in other Canadian provinces, in various American states and in other jurisdictions in Europe and elsewhere.

The Committee will also consider the problems in the field of bodily injury and of property damage in their relationships to no-fault systems and whether existing systems in other jurisdictions have resolved these problems.

It will also be relevant for the Committee to consider the impact of various no-fault systems on premiums, on reparations, on the functioning of the courts and on other parts of the insurance system.

Included in the Committee's review will be a careful study of the Variplan that has been proposed by the I.B.C. and it will also consider cost projections relative to various no-fault systems, including the Variplan.

2. Ratemaking and Underwriting

The Committee has expressed concern about the rating categories and the classification system that is presently in use by the automobile insurance industry in Ontario.

The Committee will review these matters with its consultants and with the Office of Superintendent of Insurance in order to determine the extent to which the present system is actually valid.

In order to provide the Committee with a broader perspective, a review will be made of the classification systems and rating categories that are in use in other Canadian Provinces, in various American states and elsewhere.

Of particular concern to the Committee will be the question of the validity of the present system of rating territories.

The Committee will be concerned to determine whether there is in fact such a correlation between driver offence records and accident proneness as to justify the use of some system whereby such records will be reflected in the premium that are payable, either by way of a surcharge or some other mechanism.

Provisions will be considered for the revision of the Statistical Plan so as to provide the necessary statistical information for the purpose of implementing the Committee's recommendations regarding reimbursement of the Ontario Hospital Insurance Plan.

3. Compliance and Enforcement of Compulsory Insurance

The Committee has recommended the adoption of a system of compulsory third-party liability insurance and it will conduct more detailed studies as to methods to be adopted to provide for adequate compliance and enforcement.

The Committee will also consider more detailed plans for the integration of the compulsory insurance system with the licensing system.

The Committee will also consider the more detailed implications that compulsory insurance will have in relation to the Motor Vehicle Accident Claims Fund.

4. Improving the Residual Market

The Committee has expressed its concern about the industry's methods of accommodating motorists in the residual market. Further studies will be done and recommendations made with regard to the operation of the Facility and alternative methods of dealing with this problem. Specific recommendations will then be made.

5. Review of Marketing, Administration and Claims Adjusting Costs

Many questions have been raised by the Committee concerning further details about marketing, administration and claims adjusting costs as they apply to various types of coverage, various rating categories, various deductible limits and the various elements of claims adjusting costs.

The Committee will identify in detail major cost elements and will develop overall analyses of the costs of marketing, administration and adjusting claims.

6. Comparison of Private and Public Ownership

The Committee will seek to determine in detail the elements of public ownership of the automobile insurance business and how they vary from private ownership, with a view to making recommendations on this issue.

7. Reinsurance Reporting Requirements

The Committee has expressed a concern about the apparent lack of information available on reinsurance matters, particularly with regard to the branch operations of British or foreign casualty companies.

The Committee will consider recommending the enactment of requirements that would make additional information available with regard to insurance matters.

8. Solvency and Liquidity Rules

The evidence that the Committee has received to date is not conclusive as to the appropriateness of existing solvency and liquidity rules. It will therefore investigate this matter further with a view to evaluating the present rules and recommending modifications thereto.

The Committee will also recommend more detailed methods of incorporating "in-house" rules into statutes or regulations.

9. Foreign Company Branch Office Reporting

The Committee has found that only limited information is available on the financial transactions of companies operating in Canada through branch offices. The Committee proposes to review the present reporting requirements that are applicable to branch offices and it will identify possible changes that may result in giving a more complete picture of financial operations.

10. Government Presence in Rate Setting

The Committee will consider this topic more fully in the course of its forthcoming sittings. It will identify various systems in use in other Canadian and United States jurisdictions, such as rate setting, "file and use" systems, "use and file" systems, etc. The Committee will study the merits of each system with a view to making final recommendations on this topic.

11. Responsibilities and Operations of the Superintendent's Office

The Committee wishes to review in detail the extent of the present responsibilities and functions of the Superintendent's Office in order to ensure that they are appropriate in view of changes in the magnitude and in the regulatory requirements of the industries under the Superintendent's supervision. This matter will be considered in close collaboration with the Superintendent and his representatives.

In its recent hearings the Committee undertook to examine each of the eleven topics referred to it by the First Report. In its investigations it found that a number of these topics were interrelated in that study of certain fundamental issues regarding the provision of automobile insurance provided insight into the potential for improvements in various other areas.

The Committee's Second Report on Automobile Insurance provides both specific recommendations and suggested areas for improvement in the automobile insurance system in the Province. The Committee's Report is divided into five distinct but related Parts, which are outlined briefly below. A sixth Part provides a summary of conclusions and recommendations.

In Part I, the Committee examines alternative methods of ensuring compliance with compulsory insurance, the adoption of which was recommended in the First Report and subsequently announced by the government for implementation but not before 1980. The Committee concludes with its recommendations for a "model" system of compliance and for improvements in the delivery and risk selection system which are intended to resolve the Committee's concerns about the numbers of uninsured drivers and the problems of the residual market.

In Part II, the Committee undertakes to examine what it considers to be a primary issue, alongside the issue of compulsory insurance, in guaranteeing protection for the entire Ontario community from the losses resulting from motor vehicle accidents. The Committee examines the legal basis for compensating victims of motor vehicle accidents and the emphasis which the current system in Ontario places on "fault". In its First Report the Committee expressed the view that, while many practical improvements might be made in the way the present system of loss distribution works, consideration must also be given to the alternative of a fundamental restructuring of the system to new principles of compensation. Accordingly, the Committee comments in this Part on the "no-fault" approach to accident compensation and insurance coverage.

At the present time, the principle of compensation regardless of fault has been incorporated into the Ontario automobile system to a limited extent only, by means of Accident Benefits coverage which is mandatory if third-party liability coverage is purchased. The benefits to be paid under the Accident Benefits coverage are to be enriched to provide increased protection starting in July 1978.

Part III considers a matter only briefly referred to in the First Report: the issue of governmental presence in the insurance system either as a provider of insurance coverage or as a regulator and supervisor. This topic necessarily touches upon the other four topics which make up the Parts of this Report since consideration of government insurance or private sector insurance supervised by the government must involve a review of all aspects of the automobile insurance system. Accordingly, the Committee's recommendations in this Part are shaped to some degree by its conclusions respecting the present system of insurance and the potential for improvements to be made by private companies.

In Part IV, the Committee resumes its consideration of the cost of the loss distribution system in the Province. The Committee examines in greater detail than in its First Report the major elements of cost in the automobile insurance industry in Ontario and makes recommendations and suggestions for improvements to be pursued by the industry.

In Part V, the Committee looks further at the rating classification system. In its First Report the Committee expressed concern about the rate-making process currently in use by the Ontario automobile insurance industry. In this Part the Committee reviews these concerns and the information it has collected on developments in other jurisdictions and directs general proposals for change to the attention of the industry and the Superintendent's Office.

The Committee's general comments and conclusions in these five Parts are supplemented by three background studies which describe in greater detail alternatives and proposals for significant changes to the automobile

insurance system as it operates in Ontario today. These studies are concerned with the issue of "no-fault" compensation, considered in Part II of the Committee's report, and with the issues of government ownership or government regulation, considered in Part III.

These background studies, prepared by the Committee's consultants, formed an integral part of the Committee's discussions and are included, because of their considerable informational value, as part of the Second Report. The information gained in these studies, however, does not constitute the full body of opinion and fact that has shaped the views of the Committee.

PROVINCE OF ONTARIO
LEGISLATIVE ASSEMBLY
SELECT COMMITTEE ON COMPANY LAW

THE INSURANCE INDUSTRY
SECOND REPORT ON
AUTOMOBILE INSURANCE

TABLE OF CONTENTS

	Page
LETTER OF SUBMISSION	i
PREFACE	iii
INTRODUCTION	viii
CHAPTERS	
PART I IMPLEMENTING COMPULSORY AUTOMOBILE INSURANCE	1
1. Compliance with Compulsory Automobile Insurance ...	3
2. Some Implications of Compulsory Insurance and the Compliance System on the Operations of Insurers in the Province	19
3. Ensuring the Availability of Insurance to the Driver in Ontario	27
4. The Motor Vehicle Accident Claims Fund	37
PART II AUTOMOBILE ACCIDENT COMPENSATION	
5. No-Fault Automobile Accident Compensation	43
6. Advantages and Disadvantages of the No-Fault Concept	47
7. Own-Vehicle Damage	59
8. No-Fault Automobile Accident Compensation: Conclu- sions and Recommendations	63
PART III GOVERNMENT PRESENCE IN THE AUTOMOBILE INSURANCE INDUSTRY	
9. The Experience with Government Ownership	79
10. Conclusions on Government Ownership as an Alterna- tive for Ontario	97

11.	A Government Presence in Rate Regulation	109
PART IV	MARKETING, ADMINISTRATION AND CLAIMS ADJUSTING COSTS	
12.	The Operating Cost Components of the Ontario Automobile Insurance Industry	123
13.	Opportunities for Operating Cost Savings in the Ontario Automobile Insurance Industry	127
PART V	THE RATING CLASSIFICATION SYSTEM	
14.	The Present Rating Classification System in Ontario ...	139
15.	Standardizing the Rating Classification System	147
16.	Discrimination in Rating	149
PART VI	SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS	
17.	Summary of Conclusions and Recommendations	157
APPENDICES		
Appendix A	First Report on Automobile Insurance: Conclusions and Recommendations	187
Appendix B	List of Witnesses	205
Appendix C	List of Exhibits	211
Appendix D	List of Self-Insureds	221
Appendix E	Survey of Insurance Policies of Governments, Government Agencies and Government Corporations	223
Appendix F	Police Authority to Stop Vehicles and Demand Proof of Automobile Insurance Coverage	225
Appendix G	Transfers to the Facility: 1971-1976	229
Appendix H	Amendment to Schedule E of the Insurance Act (regarding Accident Benefits coverage)	231
Appendix I	Solvency and Liquidity Rules	237
Appendix J	Responsibilities and Operations of the Superintendent's Office	245
Appendix K	Industry Operating Analysis: 1974 and 1975	253
Appendix L	The I.I.A.B.O. Agency Study	255

BACKGROUND STUDIES

One.	Automobile Accident Compensation: The No-Fault Approach	263
Two.	Government Ownership of Automobile Insurance	389
Three.	A Government Presence in Rate Regulation	477

PART I
IMPLEMENTING COMPULSORY
AUTOMOBILE INSURANCE

CHAPTER 1

Compliance with Compulsory Automobile Insurance

A. INTRODUCTION

In its First Report, the Committee commented as follows:

“The Committee strongly recommends the enactment of legislation requiring that every person who owns a licensed automobile have a valid policy of automobile insurance providing third-party liability coverage and accident benefits coverage.

The principle on which compulsory automobile insurance is based is that every person who owns an automobile that is used on public roads has a moral obligation,—and ought to have a corresponding legal obligation,—to bear his fair share of the losses that are incurred on the roads and should be entitled to benefit from the payment by other automobile operators of their fair share of such losses through their insurance premiums. This principle of reciprocal benefit and obligation is so axiomatic that it should hardly need argument or justification in order to be accepted.”¹

Since the publication of its First Report, the Committee has been encouraged by the announcement of the government on February 21, 1978 of its intention to introduce compulsory automobile insurance into the Province of Ontario. A number of problems will be encountered with implementation of this programme and in its First Report, the Committee attempted to identify some of these problems and to suggest some possible solutions. However, it was recognized that further and more detailed studies of the matter should be carried out. For this reason, the final sentence of Chapter 25, “Enforcing Compulsory Insurance—The Irrevocable Policy”, read:

“The Committee has concluded that greater weight ought to be given to the implementation of a fully effective insurance programme for the province. However, the Committee has referred the matter to its consultants for further research.”²

The Committee has now had the opportunity of considering an extensive report from its consultants which outlined implications and evaluated various alternative methods of implementing an efficient compulsory automobile insurance programme in the Province of Ontario. Furthermore, the Committee has had the opportunity to learn more about enforcement procedures for compulsory insurance in other jurisdictions and has discussed the

1. The Select Committee on Company Law, *The Insurance Industry—First Report on Automobile Insurance*, Province of Ontario Legislative Assembly, 1977, page 173.

2. *Ibid.*, page 178.

matter with industry representatives. As a result, the Committee is now in a position to review this entire topic and to make its recommendations.

The Committee's comments are set out under the four following chapters of this Part, as summarized below:

Ch. 1 *Compliance with Compulsory Automobile Insurance*

In this chapter, consideration is given to the matters related to the logistics or methods to be used to ensure compliance with compulsory automobile insurance by the drivers of the Province. The problems of "self-insurers" and religious objectors to the insurance system are discussed.

Ch. 2. *Some Implications of Compulsory Insurance and the Compliance System on the Operations of Insurers in the Province*

In order to ensure that the insurance industry functions efficiently and that implementation receives the support and cooperation of insurers, it is important to consider the problems that the industry will face in implementing compulsory automobile insurance in the Province. Some of these problems and suggested solutions make up this chapter.

Ch. 3. *Ensuring the Availability of Insurance to the Drivers of Ontario*

Since automobile insurance will be compulsory for drivers, it is imperative that they have easy access to those writing automobile insurance in the Province. Matters relating to this subject are covered in this chapter.

Ch. 4 *The Motor Vehicle Accident Claims Fund (M.V.A.C.F.)*

Even with the implementation of a compulsory automobile insurance programme in the Province it will be necessary to continue with the M.V.A.C.F. Comments concerning the on-going operations of the Fund in a compulsory automobile insurance environment are contained in this chapter.

In considering the implementation of an effective insurance programme in this Province, the Committee recognizes that compulsory automobile insurance is not new either in Canada or in other countries. In Canada, only Ontario among the Provinces and Territories remains without compulsory third-party liability insurance, although the regulations in Quebec were not effective until March 1, 1978. Many of the states in the U.S.A., virtually all European countries and many other countries around the world have enacted compulsory insurance legislation. As a consequence, the problems of "compliance and enforcement" are not new. Nearly all governments have

encountered problems with the enforcement of compulsory insurance because of the numbers of people and jurisdictions involved—drivers, insurers, licencing bodies, enforcement agencies and others. Many systems have been tried in attempts to cope with these problems.

The Committee is convinced that the majority of people in this Province will automatically comply with any compulsory insurance system that is established because most people are law abiding citizens. It nevertheless is the duty of the government to develop compliance procedures that are efficient both from the point of view of the driving public and of the government agencies involved.

There will always be those among the population who will not want to comply with compulsory insurance. Some object to the concept of insurance on religious grounds; others lack a sense of social responsibility; and still others just want to "beat the system". The attitudes of these disparate groups should all be taken into account in the design of any system of compliance and enforcement if it is to be effective.

B. THE PRESENT SYSTEM IN ONTARIO

Before considering an appropriate system of compliance with and enforcement of compulsory automobile insurance in Ontario, it might be useful to review briefly the law and the procedures and practices now in force.

Under common law in Ontario, the driver of an automobile is liable for the damage that results from his careless driving in accordance with the traditional tenets of the law of negligence. In addition, Ontario long ago imposed by statute¹ a vicarious liability upon the owner if the vehicle causing damage had been driven with his permission. As a result, the necessity of third-party liability insurance for the vehicle owner has long been recognized and widely accepted.

Nonetheless, third-party liability automobile insurance is at present voluntary in Ontario. The owner of a vehicle has the option of either purchasing third-party liability insurance coverage, the statutory minimum limit of which is \$100,000, or of making a payment of \$100 to the Motor Vehicle Accident Claims Fund (M.V.A.C.F.) in lieu thereof. The payment to the M.V.A.C.F. does not provide insurance coverage to the vehicle owner, but it does provide protection up to a maximum of \$100,000 per accident to injured third parties.

There is an exception to the alternative of either purchasing insurance coverage or paying into the M.V.A.C.F. in that certain "self insurers", such as some large companies, the railroads, Air Canada, and various

1. *The Highway Traffic Act*, R.S.O. 1970, Chapter 202, Section 132.

governmental bodies, may deposit money or securities or post a bond in an amount of \$100,000 with the Registrar of Motor Vehicles or provide their own commitment to ensure the payment of motor vehicle accident claims.

The vast majority of Ontario vehicle owners purchase third-party liability insurance coverage. Proof of insurance at the time of vehicle registration is by means of self-certification. An owner has only to complete a section of his vehicle permit to indicate that he is covered for third-party liability insurance when renewing his licence plates and it is assumed that he is insured for the term of the plates. No checks are performed either at the time of licence renewal to determine that the insurance coverage is in force or subsequently to ensure that coverage is maintained in force for the term of the licence plates. Sporadic checks to identify uninsured motorists are carried out by the police when drivers are stopped for traffic violations, at spot checks or when accidents occur.

The penalty for false statements on the vehicle registration application is \$200 and the penalty under The Motor Vehicle Accident Claims Act for knowingly making a false statement with respect to the issuance or transfer of a permit is a fine of not less than \$50 and not more than \$500 on conviction. In addition, the guilty person's licence or permit may be suspended for a period of not more than one year. Charges and penalties fall within the jurisdiction of the Ministry of the Attorney General and enforcement is carried out by the various police departments under the overall supervision of the Ministry of the Solicitor General.

Because of self-certification and the lack of rigid enforcement, some vehicle owners neither insure their vehicles nor make payments to the M.V.A.C.F. M.V.A.C.F. officials indicated the "population" of the Fund was approximately 140,000 as at March 31, 1978 or about 3% of the total of all registered private passenger and commercial vehicles. Various sources have estimated that the total number of uninsured vehicles in the Province ranges between 7% and 12%, or on average 10%, of all registered vehicles. This includes not only vehicles in respect of which M.V.A.C.F. contributions have been made, but also vehicles on which insurance policies have lapsed and vehicles for which false statements on renewal applications have been made. It is to be emphasized that there is no accurate method of determining the number of uninsured drivers so these percentages are approximate.

It is interesting to compare these percentages with similar estimates in other jurisdictions. Officials in British Columbia, Saskatchewan and Manitoba, all of which have government operated automobile insurance systems, estimate that less than 1% of the vehicles in their Provinces are uninsured. In the U.S.A., it is estimated¹ that in 1975, 13.5% of all private passenger

1. Submission made by State Farm Mutual to the Select Committee—October 4, 1977.

non-fleet automobile registrations were uninsured. Further, the Committee found in its meetings in the United States that in three of the larger states with compulsory insurance requirements, estimates of the percentage of uninsured vehicles were relatively high—Florida 17.8%, California 16.2% and Massachusetts 15.3%. High premiums, lack of adequate compliance procedures and unsolved problems of enforcement were all suggested to the Committee as reasons for these high percentages. It is apparent that the proclamation of compulsory insurance legislation in itself does not guarantee compliance.

C. PREREQUISITES OF A COMPULSORY AUTOMOBILE INSURANCE COMPLIANCE SYSTEM

While acknowledging the problems in other jurisdictions, the Committee is still satisfied that it is possible to implement a system of compulsory insurance in Ontario with only minor changes to present practices and procedures. This could be accomplished by:

- retaining the procedure whereby motorists certify on their licence plate renewal application forms that they have valid insurance in force;
- eliminating the option for motorists to pay a \$100 fee to the Motor Vehicle Accident Claims Fund in lieu of carrying insurance coverage;
- eliminating the alternative available to certain self-insurers of providing their own commitments or of depositing securities or posting a bond with the Registrar of Motor Vehicles that then permits them to depart from the requirements to maintain insurance coverage;
- relying on the law enforcement agencies to aid in the apprehension of uninsured motorists when investigating traffic violations and accidents or while conducting spot checks;
- increasing substantially the minimum penalties for owners of uninsured vehicles using the roads; and
- retaining the Motor Vehicle Accident Claims Fund to be financed by a portion of the drivers' licence fees at least for the time being.

There is no doubt that there would be fewer uninsured vehicles on the road than at present. Many vehicle owners who presently pay the \$100 fee to the M.V.A.C.F. would obey the law and obtain the required insurance coverage. The Committee believes that it is not unreasonable to assume that there may be as few as 5% of the vehicle owners of Ontario uninsured if compulsory insurance legislation was passed and no basic changes were made in the present system of compliance and enforcement.

However, the Committee has studied alternative methods of implementing compulsory insurance and **it has concluded** that a system of compliance with compulsory automobile insurance can be developed in this Province which will be more effective than the system of reinforced self-certification indicated above. Before commenting on the type of system that

the Committee envisages for Ontario, it is necessary first to define the basic requirement of an effective compulsory system, namely, that all vehicles must be insured and remain insured for as long as they are licenced to be operated in the Province. The Committee wishes to clarify this basic premise further, in the context of the present situation in Ontario regarding the following matters.

THE VEHICLES. All vehicles which require vehicle licences should be required to carry insurance. This would include private passenger, public and commercial vehicles, motorcycles, snowmobiles, mopeds and trailers. All of these vehicles can create third-party and Accident Benefit claims and should all carry the same minimum third-party liability insurance coverage.

ACCIDENT BENEFITS COVERAGE. At present the purchase of Accident Benefits coverage is mandatory if third-party liability coverage is purchased. With the introduction of compulsory third-party liability automobile insurance, the requirement to purchase Accident Benefits coverage should be retained.

SPECIAL GROUPS: SELF-INSURERS. In its First Report, the Committee commented on the special arrangements that self insurers are able to make in lieu of the standard requirements that a vehicle owner must either purchase insurance coverage or pay a fee to the Motor Vehicle Accident Claims Fund. Instead, self-insurers are permitted, in some cases, to deposit money or securities or post a bond with the Registrar of Motor Vehicles to ensure the payment of motor accident claims, and, in others, to give their own commitment to pay all claims. The Committee then went on in its First Report to comment as follows:

“Under a compulsory system of automobile insurance such as has been recommended by the Committee and particularly where the third-party liability coverage is to be in an unlimited amount, it will no longer be acceptable for self insurers to continue the practice described above and they will accordingly be expected to maintain automobile insurance coverage in the same manner as any other licence holder.”¹

In reviewing the conclusions of the First Report, the Committee is in accord with the concept that exceptions to compulsory insurance requirements are contradictory to the basic principle of fairness of loss distribution among all motorists of Ontario.

With respect to the current practice of self-insurance, the Committee is concerned that there is no review of the adequacy of the security provided by self-insurers, or of their financial ability to meet their undertaking to pay all claims. For example, the Committee has concluded that the current practice

1. Select Committee on Company Law, *First Report on Automobile Insurance*, page 175.

of filing a \$100,000 bond, irrespective of the number of vehicles exempted from insurance coverage, is unsatisfactory. Should companies who are presently allowed to self-insure be allowed the same privilege in the future, the Committee would recommend that they be required to establish proof of financial responsibility along the lines of a formula to be developed by the Superintendent.

Furthermore, the Committee has recognized that, without changes in law, self-insurers would not be obligated to provide Accident Benefits payments, nor would the adjustment of claims by self-insurers fall under the provisions of the Insurance Act and thereby under the supervision of the Office of the Superintendent of Insurance. In particular, the Committee is concerned about the ability of self-insurers to pay first-party benefits on a lifetime basis.

The Committee has also expressed concern that self-insurers are not required to share in the costs of operating essential components of the insurance system, such as the residual market mechanism and appraisal centres, and that they are not required to provide statistics on their claims experience.

The Committee has reviewed information with respect to those corporations or agencies who deposit securities with the Registrar in lieu of insurance coverage or payment of the uninsured motor vehicle fee. A list of these companies is included in Appendix D. In addition, the Committee has noted that the Motor Vehicle Accident Claims Act exempts the owner of a motor vehicle who "is a government or other body or person exempt from paying registration fees under the regulations made under The Highway Traffic Act or a municipality",¹ from payment of the uninsured motor vehicle fee and from the requirement to deposit money or securities, or post a bond with the Registrar. The Committee requested its consultants to carry out a brief survey of the insurance or self-insurance practices of federal, provincial and municipal agencies operating in the Province, the results of which are shown in Appendix E.

As a result of its investigations and its consideration of the practices of self-insurance, **the Committee recommends** that private corporations not be excluded from the requirement for compulsory insurance coverage. Furthermore, **the Committee recommends** that governmental bodies whose activities are substantially commercial, such as Ontario Hydro or Air Canada, also be required to provide proof of insurance for their motor-vehicles.

The Committee also recommends that the present exemption for governments be reviewed, so that only federal and provincial government ministries, departments and agencies not engaged in commerce be considered to

1. *The Motor Vehicle Accident Claims Act*, R.S.O. 1970, Chapter 281, Section 2.

be exempt from compulsory insurance. Municipalities, in the Committee's opinion, should be required to provide proof of insurance, since in the case of smaller municipalities the financial ability to pay large claims may be lacking.

SPECIAL GROUPS: RELIGIOUS OBJECTORS. Exception to the requirement for compulsory insurance coverage has been requested in submissions that the Committee has received from the Conservative Mennonite Churches of Ontario representing about 300 to 500 families in the Province. This is a religious community that has been long-established in Ontario. They have traditionally paid fees into the Motor Vehicle Accident Claims Fund instead of carrying automobile insurance. When losses have occurred, they have paid them by means of joint contributions raised from within their own community. They have adopted this procedure because it is against their fundamental religious conviction to rely upon the automobile insurance system. For this same reason they have asked that they not be compelled to carry automobile insurance in the future.

As a general rule, such an exception would be contradictory to the principle of compulsory insurance. However, **the Committee has concluded** that exemption from the principle of compulsory automobile insurance should be granted to this long-standing religious group. This exemption might be extended to other religious groups able to demonstrate that this belief is equally an article of their faith.

Nevertheless, other users of the road are entitled to the full protection that the established loss distribution system affords. Accordingly, **the Committee has further concluded** that the granting of exemptions to religious objectors must be conditional upon the applicants establishing that, even though they are in fact uninsured, the losses which they occasion will be paid as fully as though they were insured under all compulsory forms of insurance, including benefits that would ordinarily be paid under the Accident Benefits coverage of the present standard automobile policy, and including all first-party benefits that might be made mandatory in the future. This commitment should be established by the filing of proof of and security for the applicant's financial capacity to pay their losses. The form of such proof and the amount of such security should be determined by the Superintendent.

D. MODEL SYSTEM OF COMPLIANCE

The Committee envisages that a *model* of an efficient compulsory automobile insurance compliance system for Ontario would encompass the following salient factors:

1. The present "plate-to-vehicle" system of vehicle registration would be replaced by a "plate-to-owner" system.

2. Positive proof of the required insurance coverage would have to be provided to the licencing agent at the time of the vehicle permit (licence plate) issue or renewal.
3. The expiration of the insurance policy for a vehicle would be coterminous with the expiry of its licence plate.
4. In order to spread the work load more evenly throughout the year a system of staggered or cyclical renewals of licence plates during the year would be introduced.
5. An insurance policy would be non-cancellable before its expiry date, by either the insurer or the insured without proof of replacement coverage or the return of the licence plate to which the insurance applied.

Implementation of a system embodying these points would result in an efficient method of ensuring compliance with compulsory insurance by all vehicle owners in Ontario with the exception only of those who presented fraudulent documents as proof of insurance. It would also minimize the need to rely on law enforcement officers to police the insurance system.

Introduction of this *model* system is, however, not a simple process. In some respects it would result in problems for the industry or inconvenience for the public. These difficulties and suggested solutions are reviewed by the Committee later in this chapter and in Chapter 2. It is also evident that introduction of such a system would require the cooperation of the insurance industry and of several Ministries of Government of the Province in addition to the Ministry of Consumer and Commercial Relations which is responsible for the administration of the Insurance Act.

The Committee has been advised that a review of the vehicle registration system in Ontario is already underway by several Ministries of the Province—the Ministries of the Attorney General, Consumer and Commercial Relations, the Solicitor General, and Transportation and Communication. While the precise status of the work of this Inter-Ministerial Committee has not been made public, Phase II of their joint project has been completed and it has been indicated that the system envisaged in the foregoing is compatible with the views of that Committee.

Comments concerning each of the five points set out above, various alternatives to them and other related matters are dealt with in some detail below.

Plate-To-Owner System

The Ministry of the Solicitor General made a formal request for a change to a plate-to-owner system in Ontario in January, 1974 and the Cabinet approved this concept in principle in 1975. The majority of the Provinces with the exception of Ontario and three Atlantic Provinces presently

use the plate-to-owner system of vehicle registration rather than the alternative plate-to-vehicle system.

The Committee believes that a plate-to-owner system has many advantages in ensuring compliance with and enforcement of compulsory insurance. A licence plate would not be issued to an owner without evidence of insurance coverage. The licence plate then identifies the vehicle as being insured. The licence plate stays with the owner of the plate and is removed when the vehicle is sold or destroyed. For insurance purposes under a plate-to-owner system, the key identification is the licence plate number which is unique and not as easily confused as an owner's name. There are also many law enforcement benefits to a plate-to-owner system ranging from more effective law enforcement to increased productivity.

Compulsory third-party liability automobile insurance as recommended will mean that all vehicles which require vehicle licences will be required to carry insurance. When this prerequisite is combined with a plate-to-owner concept the principle of perennial plates for all classes of vehicles is almost indisputable. However, to implement "perennial plates" for all classes would mean a change in the method presently in use in Ontario of issuing quarterly licence plates to certain commercial and seasonal vehicles. The issue of perennial plates for all vehicles would necessitate the use of some means of identifying the month and year of expiry. It is suggested such identification could take one of many forms of decals attached to the licence plate or the windshield of the vehicle.

The Committee was advised that the Inter-Ministerial Committee reviewing the entire vehicle registration system in Ontario is studying the implementation of a plate-to-owner system of vehicle registration.

Proof of Insurance Coverage

The most effective compulsory insurance compliance system would require positive proof that the required insurance coverage is in force at the time application is made to the licencing agent for a vehicle permit (licence plate) issue or renewal. The Committee believes that effective procedures can be developed to meet this objective. Approved certificates of insurance on which the licence plate number of the vehicle owner would be indicated, would be issued by insurance companies only when a valid policy of insurance is in effect and the Registrar of Motor Vehicles would then be assured, except in the case of fraudulent certifications, that the owner of the vehicle is insured before a new or renewal vehicle permit would be issued. The procedure for recording the licence plate number on the certificate of insurance of a "first time" vehicle owner would simply require the licencing agent to note the licence plate number on the certificate, when the vehicle permit is issued. On all renewals the licence plate number would be noted on the certificate before it was taken to the licencing agency office.

The Provinces of British Columbia, Saskatchewan and Manitoba all require positive proof of insurance before vehicle permits and licences are issued to the extent that insurance is purchased at the time of the registration process. Some of the other Provinces of Canada required positive proof of insurance at one time, but now use a form of self-certification. Similarly, in the United States, of the sixteen states canvassed, twelve used positive proof of insurance at one time, although only four of these states continue to do so. The other states rely on some form of self-certification.

In Ontario, the requirement that proof of insurance be presented at the time of registration was enforced at one time but has now been abandoned. The requirement to show proof of insurance meant some inconvenience to the public because of the line-ups and delays as licencing agents checked insurance certificates and because applicants sometimes forgot or lost their certificates and had to return to the licencing office a second time. The Committee recognizes that, if positive proof of insurance is re-introduced as a requirement of vehicle permit (licence plate) issue or renewal, it must be on the grounds that enforcement of compulsory automobile insurance justifies some inconvenience to the driving public. Every effort should be made to establish procedures to minimize any such inconvenience.

The Committee views positive proof of insurance at the time of the vehicle licence issue or renewal as the most desirable or optimal method of ensuring compliance with compulsory insurance. It considers self-certification and a complex exchange of information system to be two less acceptable alternatives. As indicated, many of the states in the U.S.A. use a form of self-certification of insurance coverage at the time of application for licence plate issue or renewal. In effect, all of these states are relying on the honesty of individuals that they have the required insurance coverage in force and will keep it in force. However, the Committee has seen in its studies that, even in states with compulsory insurance laws, uninsured vehicles frequently exceed 15% of auto registrations.

Either as an alternative to or together with self-certification or positive proof of insurance, it is possible to set up procedures for the exchange of information between insurance companies and the Registrar of Motor Vehicles concerning the status of the insurance on each licenced vehicle. Consideration was given to some aspects of the feasibility of such a system by the Committee in its First Report. It was recognized that the procedures involved were very complex and the Committee concluded after discussions with computer systems consultants that a "system of enforcement, based on the 'matching' of a vast mass of paper, ought not to be adopted".¹

1. Select Committee on Company Law, *First Report on Automobile Insurance*, page 178.

Terms of Policy

The Committee believes that an effective compulsory insurance compliance system requires that the term of automobile insurance policies should be identical to the term of the vehicle permit to which the insurance applies. Presently, with the exception of certain commercial and seasonal vehicles, all licence plate renewals occur in the months of December, January and February with the vast majority in February. If the expiry date of an automobile insurance policy is not made coterminous with the expiry of the vehicle licence permit of the applicable vehicle, the procedures involved in ensuring compliance with the compulsory insurance legislation will be complicated immeasurably.

The Committee notes that the 1968 British Columbia *Royal Commission on Automobile Insurance* concluded that "studies by the Commission suggest that enforcement is made more difficult when the insurance is cancellable by the insurer, and when insurance is not coterminous with drivers' licences".¹

Staggered Renewals

Under the present annual licence permit renewal system, the problems that would be created for the insurance industry would be horrendous if all policies were to expire at the same time.

In order to alleviate the peaking of insurance and registration renewals during the month of February, **the Committee suggests** that renewals of vehicle permits and insurance policies be staggered throughout the year.

Staggered renewals would require some easy means of identifying that a valid permit and applicable insurance coverage are in force for all vehicles on the road at any time. There are various alternative means of indicating the date of expiry, for example:

1. The last digit on the licence plate could be used to indicate the month of renewal: 1 for January, 2 for February, and so on; with a sticker similar to the one presently in use in the Province to indicate the year of expiry.
2. Decals might be used in one of many forms, for example, alpha or colour coded or dated; in metal tags or stickers; to be attached to the windshield or to the licence plate.

The preferable procedure, and the one suggested for Ontario, when licence permit and compulsory insurance are combined in the vehicle registration system, would be to use decals attached to the licence plate. Separate decals could indicate the month of expiry, by name; and the year of expiry,

¹ *Royal Commission on Automobile Insurance, Province of British Columbia, July 1968, Vol. II, page 571*

by colour as presently used in Ontario, or by year as used in many of the states of the U.S.A.

By staggering renewals the work of the Motor Vehicles Branch would be spread more evenly through the year and it should be possible to keep records more current than at present. The introduction of such a system would require that alternative arrangements be made to the present practice of operating temporary local licencing agencies for a short time each year. The convenience of the alternative arrangements for the public must be considered. The Committee was advised that the Inter-Ministerial Committee reviewing the entire vehicle registration system in Ontario is considering this problem along with all of the implications of implementing staggered renewals.

With staggered renewals, the inconvenience to the driving public should be minimized since the potential line-ups and delays at the time of registration would be significantly shorter than is now the case with the February peak of renewals.

Non-Cancellable Policies

One of the basic prerequisites of compliance with compulsory insurance legislation would be to ensure that compulsory insurance coverage is maintained for as long as the applicable vehicle is licenced to be used in the Province of Ontario. This would imply, conversely, that if insurance coverage is not in effect then the vehicle should not be considered to be licenced. It would appear to the Committee that the best way to ensure that this prerequisite is fulfilled is to insist that, once issued, insurance policies would be irrevocable and non-cancellable by either the insured or the insurer. An exception would be made only if some form of "guarantee" was provided that, once the insurance was cancelled, the vehicle would not be used in the Province, as it would no longer be licenced.

Under a plate-to-owner system licence plates would remain with the owner of the plates. In order to cancel his insurance before its expiry date, it would be necessary for him to surrender his plates when disposing of his vehicle, either on its sale, if no subsequent acquisition is involved, or on its destruction. It is envisaged that a certificate or similar document would be completed by the Registrar of Motor Vehicles to evidence the fact that the licence plates had been turned in by the owner. This certificate then would be used to cancel the insurance and to support any premium refund. It is not however, intended that the return of the licence plate would be required in the case of expired coverage, for example, in the case of seasonal vehicles.

The Committee also proposes that an exception might be accommodated in the case of an insurer wishing to cancel for reasons of non-payment of the insurance premiums by the insured, but only if a method could be developed of effectively cancelling the vehicle permit as a result of the cancel-

lation of the compulsory automobile insurance policy. This matter requires consideration since the Committee recognizes that problems may be created for the insurance buying public and the insurance industry with the introduction of irrevocable and non-cancellable policies as discussed in some detail in Chapter 2 of this Report.

While the Committee does not consider these problems to be insurmountable, it is, however, of the opinion that a study of alternatives to the irrevocable policy should be conducted. Therefore, **the Committee recommends** that the Inter-Ministerial Committee in its review of the vehicle registration system be requested to study the feasibility of a system of integrating cancellation of vehicle permits with notice of cancellation of automobile insurance coverage.

Under this system, insurance companies would be required to inform the Registrar of Motor Vehicles concerning the cancellation of any compulsory automobile insurance policy; this notice would then be matched with the Registrar's computer file of registered vehicles. Although the Committee in its First Report concluded that such procedures were very complex, it nevertheless believes they merit the further attention of the Inter-Ministerial Committee.

Furthermore the Committee recognizes that an integral component of the above system must be an effective method of enforcing licence plate cancellation, either through seizure of unsurrendered licence plates or through significant penalties, as suggested in the following section, for those owners who continue to drive uninsured and unlicensed vehicles.

The Committee emphasizes that, while it endorses further study of a system of permitting cancellation of automobile insurance for non-payment of premiums, it continues to believe that the *concept* of an irrevocable or non-cancellable policy coterminous with a valid licence plate is basic to a truly efficient compliance system for compulsory automobile insurance.

E. ENFORCEMENT OF COMPULSORY INSURANCE

The specific enforcement procedures required to ensure compliance with compulsory insurance legislation are dependent mainly on the procedures that are used to satisfy the licence issuing authorities that valid insurance is in force at the time of vehicle registration. With positive proof of insurance at the time of registration, the need to rely on subsequent enforcement procedures is reduced substantially. On the other hand, greater reliance must be placed on enforcement procedures during the year to apprehend uninsured drivers if other methods of proof of insurance, such as self-certification, are used and also if it is decided to maintain the insurer's right to cancel coverage.

In theory the aim of an efficient comprehensive compulsory insurance programme should be to eliminate uninsured vehicles while minimizing the

need to rely on law enforcement officers to police the insurance system. Studies have indicated that law enforcement officers do not consider that one of their priorities should be to confirm that drivers are insured when they conduct spot checks, apprehend traffic violators or investigate accidents. Instead, in many jurisdictions, there appears to be considerable reluctance on the part of law enforcement agencies and the courts to prosecute and to impose fines, licence cancellations and jail terms even when called for in the enabling legislation. Rather, the authorities in many instances prefer to apply nominal penalties, if any, to the uninsured motorists who are apprehended.

Examples of the types of penalties imposed in various jurisdictions for not having insurance are as follows:

1. In Nova Scotia fines of \$50 or 7 days in jail are imposed for the first offence, \$100 or 14 days for the second offence and \$250 or 30 days in jail for the third offence.
2. In Alberta the penalties are nominal.
3. In New Jersey the maximum penalty is a two-year driver suspension or 3 months in jail. There is only one known case where the maximum jail sentence has been imposed.
4. In Michigan a criminal charge is laid if an individual is not able to produce proof of insurance within 72 hours. The police have found that it is almost impossible to get a conviction, thus they have given up enforcing this law.
5. In Florida the maximum penalty is the loss of a driver's licence and licence plates.

Regardless of the compliance procedures that are introduced, there will always be uninsured vehicles. With the introduction of compulsory insurance legislation in the Province of Ontario, an extensive advertising campaign should be carried out to acquaint the driving public with the programme and the compliance procedures. In addition, the enabling legislation should include provisions for significant minimum penalties for non-compliance designed to penalize the uninsured driver severely enough that he would be reluctant to commit a second offence. The penalty for not having insurance or falsifying insurance is **recommended by the Committee** to be a minimum of not less than twice the approximate cost of the insurance, and should include licence suspension.

Some have suggested that, with the passing of compulsory insurance legislation in Ontario, the police should be allowed to lay charges on the spot against uninsured drivers, with the provision that the individual be given 72 hours to produce evidence of insurance coverage. The driver in the latter instance should be charged with the offence of not having insurance

coverage while driving and should not be allowed to purchase future coverage as proof of insurance.

The Committee noted that the authority for police officers to stop vehicles and demand proof of insurance is contained in Section 3 of *The Motor Vehicle Accident Claims Act* and in Section 55 of *The Highway Traffic Act*. A review of the provisions of these Acts is included in Appendix F. **The Committee has concluded** that there is value in setting out clearly in the Insurance Act the specific authority for police to stop a vehicle for the purpose of checking for compulsory insurance coverage and recommends that the Minister make such changes to the Act.

CHAPTER 2

Some Implications of Compulsory Insurance and the Compliance System on the Operations of Insurers in the Province

In order to ensure that the insurance industry functions efficiently and the implementation of a compulsory insurance programme in the Province receives the support and cooperation of insurers, due consideration must be given to the problems that would be created for the industry under the *model* compliance system. In addition, the implementation of compulsory insurance will cause some inconvenience and create some problems for the motorists of the Province. Some of the problems that have been identified are discussed below along with tentative solutions to them. Discussions have been held by the Committee and its consultants with industry representatives and others in an effort to isolate difficulties that would arise for both the insurers and the insureds with the implementation of compulsory insurance in the Province as proposed.

Some of the major problems that insurers will face, together with a few problems that will confront the insureds, have been reviewed by the Committee and are set out below together with remarks concerning each.

- (a) The major problem the industry is concerned with is non-payment of the insurance premiums by the insured.

Since a keystone of the *model* compliance system considered in Chapter 1 is a non-cancellable or irrevocable insurance policy, it is implied that an insurer is entitled to be paid the premium for the coverage it is providing. An insurer must be paid the premium due to it in advance or it must be prepared to accept the responsibility for the credit it grants to its customers. In effect, the purchase of automobile insurance will differ from normal business transactions in that the vendor (the insurer) will not have the right of repossession of his product if his customer does not pay for it once the product has been delivered to him. It is, therefore, imperative that the vendor either be paid in cash in advance or be satisfied that the purchaser will make good the purchase price. Representatives of the industry have suggested that companies will place the onus of responsibility for collection of premiums on their agents. If they do so this would be entirely a matter between them and their agents and should have no effect on the validity of the policy or its coverage.

In spite of the best efforts of insurers, it is likely there will always be situations where vehicle owners are able to obtain insurance without the payment of the appropriate premiums for the coverage they require. While non-payment of all or a portion of the proper premium by an insured should, under the *model* system, have no effect on the cov-

erage in force once a policy has been issued, it may be possible for procedures to be developed, ancillary to other collection procedures of amounts due by delinquent motorists, to permit the collection of unpaid premiums and thus aid the industry. The possibility of implementing such procedures is beyond the scope of this report and is more clearly a matter to be considered by the Inter-Ministerial task force reviewing the entire matter of motor vehicle registration.

- (b) With the requirement set out above that premiums be paid in advance for compulsory insurance coverage, many individuals will face the problem of having to arrange methods of financing the amount involved. It has been estimated by insurance industry representatives that a significant portion of the motorists of the Province presently arrange some method of financing their insurance premiums. In many respects this problem will be no different under compulsory insurance than it is today.

Presently a motorist when purchasing insurance, if unable to pay the full annual premium at one time, may arrange to pay semi-annual, quarterly or even monthly premiums to his insurance company at effective rates that increase as the period is shortened. Further, motorists have the alternative of purchasing short-term licence plates with appropriate seasonal insurance coverage. Doubtless many motorists arrange to finance their auto insurance premiums through regular borrowing channels from financial institutions.

With the implementation of the *model* compliance system, some insurance companies will be prepared to grant terms to their customers. Failing this accommodation, motorists will have to find some other means of financing their premiums or, if this course does not appeal to them, they should be given the opportunity to renew their licence plates for less than one year and to purchase the required insurance coverage for the shorter period to expire at the same time as the licence plates.

- (c) In spite of all the safeguards that individual insurance companies will be able to build into their procedures for checking applications for insurance, there are bound to be cases where motorists will be issued policies and hence be able to renew their licence plates based upon errors in or misrepresentations of facts on their applications. When notified of the mistakes in premiums that result, it is probable that there will be some who will ignore the request to pay the additional amount.

There is no easy solution to this problem of an irrevocable policy system. However, the industry itself may wish to share such problems by perfecting their present policy of pooling such risks whenever they are identified during the term of the insurance. Further, depending upon the detailed system that is eventually developed for the implementation

of a plate-to-owner system in Ontario, it may be practicable to set up special procedures whereby such motorists who misrepresented the facts on their applications and hence underpaid their premiums would be denied the right of renewal of their licence plates until the unpaid premiums were settled. Protection of this type to the insurance industry would seem reasonable and could possibly be tied in with procedures that might require payment of any outstanding fines before permits would be renewed.

- (d) Since a motorist must maintain the required insurance coverage at all times, it would be important for him to receive notice of the expiry of his current coverage several weeks, say six, in advance of the expiration of his licence plates and his insurance. Sufficient notice must be provided to an insured to permit him to consider changing insurers for whatever reason he might have. In most cases insurance policies would be written for one year. During the year it would be difficult to change insurers. An insured's mobility would be considerably reduced and there would be the possibility that an individual might be denied some freedom of choice of insurers. By providing notice of expiry of an insurance policy six weeks prior to the expiry of the coverage, the insured would have adequate opportunity either to renew his insurance or to seek the appropriate coverage with another insurance company.
- (e) The Committee in its First Report recommended that motorists should be given a period of ten days grace after the renewal date of their insurance in order to make payment to their insurance company. To quote:

“Accordingly, a provision should be included in the standard automobile policy that, notwithstanding the fixed termination date set out in the application form, the policy will continue in force for ten further days unless the policy was formally terminated by due notice given by either the insurer or the insured prior to the end of the fixed term set out in the application form.”¹

The Committee's further deliberations have made it clear that this recommendation is incompatible with the concept of the *model* system of compliance with compulsory insurance as proposed and the requirement that positive proof of insurance be provided at the time of licence plate renewal.

- (f) Some insurers in the Province presently do substantially all of their business on the basis of six month policies. Since the system of compliance with compulsory insurance as proposed envisages that the expiry of insurance policies would be coterminous with the expiry of the licence plates of the vehicles involved, all companies doing business in

1. Select Committee on Company Law, *First Report on Automobile Insurance*, page 47.

the Province would likely have to be prepared to issue annual policies.

It is not intended, however, that companies would be precluded in any way from continuing to sell policies with terms of less than one year. In order to accommodate motorists taking advantage of this alternative, it is anticipated the present option available to them to purchase short-term licence plates would be used more frequently.

- (g) Special consideration would have to be given to the treatment of fleets covered under one insurance policy.

Normally fleets would be covered under a policy with one expiry date for all vehicles. One alternative that has been considered to identify the expiry of a vehicle permit is to use the last digit of the plate to indicate the month of expiry. If this system were enforced, it would mean that all vehicles in a fleet covered by a policy with one expiry date would have to have the same digit identification on the licence plate. This would be impractical. To indicate the expiry of the vehicle permit it would be preferable, in the Committee's opinion, to use a decal system with appropriate stickers or tags to be attached to the licence plate of the vehicle on which to indicate both the month and year of expiry to the permit and the related insurance coverage.

- (h) As has been noted previously, special groups such as certain large companies and agencies of the crown are presently able to depart from the normal requirements of either purchasing insurance coverage or paying into the Motor Vehicle Accident Claims Fund by providing their own commitment or by posting a bond or placing securities with the Registrar of Motor Vehicles. With the implementation of compulsory insurance and in particular if the recommendation contained in the Committee's First Report concerning unlimited third-party liability coverage is implemented, it would be undesirable to continue any special arrangements, excepting only for Federal and Provincial governments as previously specified and for the members of exempted religious groups such as the Conservative Mennonite Churches of Ontario, whose need for exemption has been discussed above.¹

All vehicle owners in the Province other than exempted religious objectors and specified government bodies would have to arrange to have insurance coverage as required regardless of their intentions not to resort to the insurance system to satisfy any claims in which they might be involved. Any accommodation the industry might be prepared to make to these special groups could not negate in any way the requirement that every person who owns a licenced vehicle must have a valid

1. *Supra*, page 10

policy of automobile insurance providing third-party liability coverage and Accident Benefits coverage.

- (i) The *model* compliance system proposed would involve the staggering of renewals of both licence plates and insurance policies throughout the year. The transition to a staggered renewal system would present some problems to the insurance industry and inconvenience to some motorists.

The transition might be handled best by having insurers arrange that all policies in force (except those that presently expire at a month end) expire at the end of the month prior to their present expiry date with appropriate adjustments or refunds made to motorists as required. All motorists whose insurance expires on February 28 would renew their licences as they would normally do now. All other motorists would be required to renew their licence plates for the period from February 28 to the month end of the expiry of their insurance policies and then renew their licence plates along with their insurance once again effective at that month end.

- (j) The problems faced by an owner of a commercial vehicle or of a seasonal vehicle who requires only a short-term licence would be no different under compulsory insurance than at present with the exception that he would have to provide positive proof of insurance at the time he renewed his licence plates indicating the required coverage was in force at least to the date of the expiry of the licence plates. A vehicle owner would then be provided with a month and year decal to indicate his licence plate was valid and his vehicle was insured.
- (k) Transactions involving a new or used car purchase by a first time buyer could not be completed and the vehicle licenced until the purchase of the required insurance coverage had been arranged and proof of insurance provided to the Motor Vehicle Registration office. Further, in the event of a vehicle owner moving out of the Province permanently, it would be necessary for him to surrender his licence plates and obtain a certificate from the Motor Vehicle Registration office that he had done so before an insurance company could cancel his insurance and make any appropriate refund to him. Meanwhile, depending upon the jurisdiction to which he had moved, the motorist might find that he would have to have double coverage for a period of time.
- (l) It would be more convenient for motorists to change insurers between licence plate and renewal dates.

Under the *model* compliance system, it would be necessary for a motorist who wished to do so to arrange replacement coverage as required and obtain a certificate of insurance from his new insurer. He would then have to present it to the Motor Vehicle Registration office to ob-

tain a certificate authorizing his previous insurer to refund to him any portion of the premium that might be due to him. In other words, the new insurance would have to be in force before the old insurance could be cancelled.

- (m) Similarly it would be necessary for a motorist to surrender his plates and obtain a certificate from the Motor Vehicle Registration office before he could obtain any refund of premium if he sold his car and did not replace it, if it was demolished and not replaced, or if it was decided for any other reason not to use the vehicle for some period of time and it was "put on blocks".
- (n) Problems might be created for the insurance industry when a motorist traded in his vehicle and purchased a new one that might involve an additional premium.

At present, the company would have the option of cancelling the policy for non-payment of any incremental premium. With non-cancellable policies this recourse would no longer be available to insurers. It is difficult, however, to visualize many circumstances in which a motorist would be unwilling to pay the increased premium since if he is upgrading his vehicle the additional premium would relate to collision and comprehensive coverage and in the event of any damage to the vehicle it would be the motorist who would suffer as his claim might be refused or discounted because of the non-payment of premiums due.

- (o) It has been suggested that if policies cannot be cancelled under a compulsory insurance compliance plan, problems might be created for the industry because motorists may either become incapacitated or change circumstances during the period the policy is in force and that if these changed conditions were known to the insurer he would either cancel the coverage or at least insist on an adjustment of the premium.

In many respects the possibility of such events occurring and an insurer not knowing about them would not change merely because of the introduction of compulsory insurance. If, however, insurance cannot be cancelled by an insurer and other means of trying to obtain restitution fail, it is suggested, as in the case of misrepresentations on application, it might be possible for the industry itself to try to solve some portion of this problem by perfecting their present policy of pooling such risks when they are identified. Further, it might be possible for procedures to be set up to aid the industry to collect unpaid premiums under such circumstances at the time of the renewal of licence plates.

At the conclusion of its hearings the Committee met with senior representatives of the automobile insurance industry to discuss the implementation of compulsory insurance in the Province and, in particular, the related problems the industry could identify and the solutions they would suggest.

During these discussions and in a subsequent written submission to the Committee the industry did not raise any significant matters that had not been considered by the Committee during its deliberations. While the industry made it clear that they would prefer, in general, to maintain the present system by reinforcing self-certification, the Committee was pleased to note at the conclusion of the industry's submission that "any control mechanism can be accommodated and would receive the traditional full cooperation of the Insurance Industry."¹

After reviewing the practicable aspects of a compulsory insurance system that incorporates the five points set out in Chapter 1 as a *model* system of compliance, **the Committee has concluded**, with the exception of the condition that follows, that such a system should be implemented in Ontario.

The Committee's recommendation is conditional on the requirement for further study in the area of alternatives to the irrevocable policy. However, should study into this matter indicate that a satisfactory integration of vehicle registration cancellation with insurance coverage cancellation cannot be established, the Committee is convinced that solutions to the difficulties can be found and that the irrevocable policy should be included as an integral part of the compliance system for compulsory insurance.

1. Submission of the Insurance Bureau of Canada to the Select Committee on Company Law, "Re: Enforcement of Compulsory Insurance Law", Toronto, March 14, 1978.

CHAPTER 3

Ensuring the Availability of Insurance to the Driver in Ontario

It is axiomatic that, if automobile insurance is to be made compulsory in the Province of Ontario, licenced drivers must be able to purchase the coverage they require easily. To fulfil this requirement is not a simple matter. There are problems caused by the geography of the Province; by the capacity of individual insurance companies to write all of the automobile insurance that applicants may wish to place with them; by the desire of each company to select only the best risks for its account; and by many other factors.

While most drivers and vehicle owners in the Province are served adequately by the present insurance system, the Committee, in its First Report, dealt with some of the frustrations faced by the minority in obtaining insurance and some of the problems the industry faced in attempting to provide insurance to all drivers of the Province including those who were identified as "high risk". In the process of its review the Committee made the following observation: "the problem is nevertheless serious because of the importance of automobile insurance both to those who seek it and to those who may have to look to it for compensation".¹

The problems relating to the "availability of insurance to the drivers of Ontario" are considered in this chapter under three headings—Marketing, Underwriting and Rating. Some matters concerning each of these aspects of availability were dealt with in general terms in the First Report but are explored by the Committee in more detail in this Report.

Logically, any review of the question of availability of insurance must first consider matters relating to the alternative means by which an insured or his agent will have access to insurers to provide him with the insurance coverage he requires. These matters are dealt with under Section A of this chapter, headed "Marketing".

Depending upon the method of marketing selected, the insurers will face varying problems concerning the proportion of individual risks they may either want or be able to retain for their own account. Matters relating to risk retention and pooling of undesirable risks are dealt with under Section B, headed "Underwriting".

Premium rates for a specific insurance coverage are presently established based on the average driver with similar characteristics, including the area in which he resides, his age, the use to which he puts his vehicle, his accident record, and other factors. However, there is likely no such person as the "average" insured in any one category. Hence one-half of the people

1. The Select Committee on Company Law, *First Report on Automobile Insurance*, page 116.

in each category are better risks and one-half are worse risks than the average. Each insurer adopts underwriting procedures or risk selection practices designed to obtain more of its share of the "better than average drivers", thereby reducing the claims it will have to pay and thus improving its results. In effect the premium rates charged to better than average drivers in any category are likely to be more than adequate and the premium rates charged to the below average drivers are likely to be less than adequate. In the opinion of the insurance industry the entire matter of appropriate premium rates to be charged to "high risk" drivers forms an integral part of any consideration of availability. This subject is dealt with in Section C of this chapter, headed "Rating".

A. MARKETING

There are in effect only four alternative methods of marketing insurance. For ease of identification they might be described as—free risk selection; take-all-comers; exchange/assignment; and a facility association which is known in some jurisdictions, such as Florida, as a joint underwriting association or J.U.A.

Free risk selection, the present system in Ontario, requires the vehicle owner or his agent to contact different insurance companies until one will accept him as a customer. If the insurance agent runs out of companies to which he has access, the vehicle owner is left to find a new agent or to contact an insurance company on his own.

A *take-all-comers* system would require each insurance company to accept all applicants. While the present system in the Province of Ontario is basically a free risk selection system, it tends towards a take-all-comers system because most companies, fearing adverse publicity and the possibility of political and other pressures, accept the applications of motorists who indicate they have been having difficulty obtaining coverage.

A third alternative, known as the *assigned risk plan*, operated in Ontario until 1967 when it was replaced with the present Facility. Under this and similar plans, an agency or exchange is set up by the industry to allocate to insurers, on a cyclical basis, the coverage of each person who contacts it. Under this system, anyone who is experiencing difficulty in obtaining insurance can contact the exchange directly or through his agent and be assigned to a company. These assignments are allocated to each company based on the share of the total insurance each writes in the Province.

The final alternative is a *facility association* or joint underwriting association. Under this marketing system, several companies become servicing carriers available to those who are experiencing difficulty in obtaining insurance coverage. Each agent selects one of these servicing carriers to write his "residual" business. The agent then sends to this company the business he has had difficulty placing through regular channels.

There are a number of criteria that may be used to assess the advantages and disadvantages of each of these marketing alternatives.

- (a) Is the availability of a market guaranteed?

The take-all-comers, exchange/assignment and facility association approaches would all guarantee that a motorist would be able to contact an insurer who would provide the insurance coverage he wanted. Only under the free risk selection alternative is it possible that a motorist might not be able to contact an insurance company prepared to take his business.

- (b) Would it be necessary for a motorist to place his insurance business through an agent?

Only in the case of a facility association (J.U.A.) is it necessary for a motorist to place his insurance business through an agent if he is unable to obtain coverage through other contacts available to him. The facility association plan is based on the ability of each agent to select one of several companies who act as servicing carriers for the residual market. The agent then is able to send to the company he selects the business he has had difficulty placing through his normal channels.

- (c) Is an agent dealing with a company of his choice for all of his business?

Under a free risk selection, take-all-comers and facility association approach an agent is dealing regularly with the same company. However, under an exchange/assignment plan, the business an agent is having difficulty placing through his regular channels is allocated to insurers on a cyclical basis based upon the proportion of the total insurance each company writes in the Province. There is no guarantee that this business will be placed with a company with which the agent has done business previously.

- (d) Is it possible for any company to be forced to write a disproportionate share of the high risk market in any one category?

If for any reason an individual company should set its premium rates for any one category significantly lower than its competitors, it would be possible for that company to be forced to write a disproportionate share of the market for that category under a take-all-comers plan. If the company involved had made a significant error in its calculations it might suffer losses as a result. In the case of free risk selection a company would be able to turn down any business that it did not wish to write for any reason. In the case of the exchange/assignment and facility association there would be no need for any one company to take more than its share of high risk business since a mechanism for sharing any such business with all other insurers is inherent in these plans.

- (e) Is it possible that the capacity of an individual insurance company to write insurance would become a matter of concern? If so, this would have implications related to solvency.

For the same reason that it is possible for a company to receive a disproportionate share of the high risk market under a take-all-comers plan, it is possible that the capacity of a company as measured by the various normal solvency tests could present a problem. Under the free risk selection system no such problem would exist since a company would be able to reject any business it did not wish to write. Likewise it is unlikely that the capacity to write business would present problems under the exchange/assignment or facility association plans.

- (f) Is after sales service likely to suffer?

It is most probable that the service an insured would receive during the period his policy is in force would be best under the free risk selection and take-all-comers systems. It is probable that the level of service would be lowest under the exchange/assignment plan.

From a review of the foregoing, it was apparent to the Committee that each marketing alternative has some deficiencies. Some have also suggested that there is a stigma that goes along with the transfer of a motorist to the exchange. If this or other criteria were added to those indicated above, even more differences could be developed.

It would seem that the major deficiency of the free risk selection approach is that it provides no guarantee of availability of a market to the motorist or his agent. The significant deficiency of the facility association plan is that a motorist is denied direct access to the market if he has difficulty getting the insurance coverage he wants. He must place his business through an agent under the J.U.A. or facility association system. The exchange/assignment plan has been tried and rejected in Ontario and it is recognized that it is likely to provide the poorest after sales service to the insured. The take-all-comers plan has the disadvantage that any one company might be forced to take more than its proportionate share of high risk business. Therefore, its capacity to write business could be an important consideration unless it were possible to devise means of reinsuring portions of its business to ensure its solvency.

The Committee views a marketing system which denies the customer access to the insurer of his choice to be unacceptable, particularly after the enactment of compulsory insurance. Accordingly, the Committee is of the opinion that the take-all-comers plan would serve the driving public of the Province best, if the potential problem of an individual company's capacity to write business could be overcome.

B. UNDERWRITING

In the context of this section and as it relates to the availability of insurance for drivers in Ontario, underwriting is concerned with risk retention by the insurer. There will always be high risk drivers in each driver classification category, that is those drivers that each insurer would prefer to avoid and leave to his competitors to service. Nevertheless, the Committee emphasizes that these "high risk" drivers must be able to obtain insurance under a compulsory insurance system.

Regardless of the method of marketing that is recommended with the passing of compulsory insurance legislation, consideration must be given to the most appropriate risk retention alternatives compatible with the marketing system selected.

There are three basic underwriting alternatives for the industry in the handling of the high risk or residual market. On the one hand, it is possible to require that each company retain for its own account all of the business it writes. At the opposite pole, arrangements could be made to permit each company to pool 100% of the risk on any business it did not wish to retain, with the net cost of any business it transferred being allocated among all insurers either on the basis of the share each has of the total business written in the Province or on some other appropriate basis. Between these two extremes there is the third alternative, defined by an entire range of possibilities wherein a portion of the risk is pooled and the balance is retained by the company accepting the business originally. The Facility as operated in the Province of Ontario at present is an example of the latter with, in most cases, 85% pooling and 15% retention by the company writing the policy.

The advantages and disadvantages of 100% retention and 100% pooling with the implementation of compulsory insurance were compared by the Committee on the following basis:

- (a) Is an individual company encouraged to accept all applications for insurance?

With the possibility of 100% pooling, generally, an insurance company would accept readily all applications for insurance made to it. On the other hand, if a company were forced to retain all the business it wrote, it would want to be very selective about the business it placed on its books.

- (b) Would it be possible for any company to get a risk larger than it might normally want to accept?

Without the ability to pool certain risks there is always the possibility that a company, particularly a small one, might be faced with a risk larger than it could safely handle. It would be forced to resist writing such business and might even have to cease writing some types of automobile insurance business altogether.

Several matters became apparent to the Committee when questions relating to underwriting, in the context used in this section, were considered together with each of the four marketing alternatives set out previously. The Committee recognized that the marketing disadvantages of free risk selection in ensuring the availability of insurance coverage to drivers would not be offset with pooling. On the other hand, the major disadvantage of the take-all-comers marketing system, from the point of view of the potential capacity problems of individual companies, could be overcome with 100% pooling.

The Committee recognizes that the industry as a whole may not be enthusiastic about 100% pooling as a solution to the capacity problem of take-all-comers, since it is conceivable that through errors of judgement or miscalculations, an individual company might underprice the coverage in a particular category and yet be able to minimize its potential losses by transferring some of the consequences of its mistake to the rest of the industry through 100% pooling of the risk. Carried to its extreme, one portion of the driving public could be subsidized by all other drivers. Should the industry adopt 100% pooling as an alternative to risk retention, the Committee is persuaded that, as a minimum, procedures would have to be set up whereby the Superintendent of Insurance, either on his own or on the basis of complaints from within the industry, could investigate "bad faith" or grossly inadequate rates and have them corrected if necessary.

C. RATING

Many in the insurance industry consider that the problems concerning the availability of insurance to all drivers of Ontario are interwoven inseparably with matters relating to the premiums to be charged to the high risk drivers making up the residual market; and with the question whether this market should be self-sufficient or subsidized in part by the majority of drivers who, the companies have decided, are better risks.

At present, under the free risk selection system, the industry attempts to resolve the problem of the residual market by sharing risks through the Facility. Normally risks transferred to the Facility are at the premium rates charged by the company accepting the original business. Currently, surcharges are made only on risks transferred to the Facility for drivers with poor accident and/or driver conviction records.

Recently the industry has proposed as an alternative to the Facility, the Facility Association, which would have its own rate manual. In other words, a servicing carrier for the residual market would be permitted to have two rate manuals, one that it would apply to its regular customers, and another that it would use for motorists who are having difficulty obtaining insurance through regular channels. The rates in the residual market manual would be

set above average voluntary market rates for each classification of driver, in order to make the Facility Association self-sufficient.

The Committee, however, finds that it is difficult to rationalize the concept of objective ratemaking based on common historical data with the concept of a company having two rate manuals applicable to drivers who for statistical purposes fall in the same category. The Committee recognizes a somewhat similar situation under the exchange/assignment plan, wherein a motorist may find his application rejected by one company and may then be assigned to another with an entirely different rate structure than the company to which he made application. It is only under the take-all-comers marketing approach with a company using its own rate manual to quote premiums for each category of business it writes, that the Committee believes that the insured's ability to "price-shop" is maintained.

While the high risk driver will continue to be a problem to insurance underwriters, it is a long standing precept in the Province of Ontario that no driver should be ruled off the road because of the cost of insurance. Under compulsory insurance, there would seem to the Committee to be only one acceptable solution. **The Committee has concluded** that categories of drivers should be broadly enough defined that appropriate and acceptable premium rates for each category of driver can be determined by each insurer. All drivers in a category should then be quoted the same premium by an insurer with the understanding that the risks an insurer accepts that are "high risk" in the opinion of the company's underwriter could be pooled and shared with others in the industry in proportion to the share of the total business each writes in the Province.

Since insurers are precluded from ruling bad drivers off the road, the law enforcement authorities should. In this regard, reference should be made to Chapter 20 of the Committee's First Report in which the establishment of Driver Review Boards was recommended.

D. CONCLUSIONS: MARKETING COMPULSORY INSURANCE AND THE RESIDUAL MARKET MECHANISM

The Committee, in the preceding sections headed Marketing, Underwriting, and Rating, has reviewed the alternative methods of guaranteeing availability of compulsory insurance. The Committee has expressed the view that the take-all-comers plan would serve the driving public of the Province best, by providing the customer with direct access to the insurer of his choice at the rate ordinarily charged by that insurer for the classification into which the insured falls. It has also noted that 100% pooling of residual risks can be applied as a solution to the potential capacity problem under the take-all-comers approach.

As a result of its deliberations, **the Committee has decided to recommend** that the automobile insurance industry adopt the take-all-comers prin-

ciple in marketing compulsory insurance. The industry must consequently be prepared to undertake 100% pooling of residual risks. The Committee recognizes that alternative arrangements can be developed to control participation and share costs within the pooling system. Accordingly, **the Committee has concluded** that the industry should be free to determine the structure of the pooling mechanism required to implement the take-all-comers approach.

It is implicit in the foregoing recommendations that the premium chargeable for high risk drivers should be the company's published rate for that risk and there must be no surcharging merely because the risk is pooled.

With the adoption of 100% pooling as an alternative to risk retention, **the Committee is persuaded** that, as a minimum, procedures would have to be set up whereby the Superintendent of Insurance, either on his own or on the basis of complaints from within the industry, could investigate "bad faith" or grossly inadequate rates and have them corrected.

The Committee further recommends that the Superintendent of Insurance be given the right and the obligation to evaluate the operations of the residual market pool and carry out analyses of its population. It is the intention of the Committee that the Superintendent monitor the operation of the pooling mechanism and issue an annual report dealing with his findings. To aid in this task, the Facility or other residual market mechanism, including the pooling mechanism under a take-all-comers approach, would be required to submit information to the Superintendent on a regular basis.

In addition, **the Committee recommends** that at the end of five years, a special summary report, evaluating the success or failure of the residual market mechanism in serving the public, should be prepared by the Superintendent's Office and provided to the Minister to be tabled in the Legislature. In the meantime, if the situation warrants such action, the Superintendent should be obligated to formulate recommendations and submit them to the Legislature.

Finally, **the Committee recommends** that all insurers licenced in Ontario be required by legislation to share in the costs of operating the residual market mechanism. At present, participation in the costs of operating the Facility is one of the conditions of obtaining a licence to operate in this Province, but the condition is not a legislated requirement. Because the residual market mechanism is essential to the availability of compulsory insurance, the Committee maintains that participation in its costs be made mandatory.

The above three recommendations apply whether or not a take-all-comers approach is implemented. The importance of these recommendations would in fact be greater under the alternative methods of marketing compulsory insurance.

Should implementation of compulsory insurance by the government of the day not include the requirement for a take-all-comers approach to marketing, attention must be given to ensuring that the selected marketing-pooling alternative will serve the interests of the public. In this regard the Committee offers the following observations and recommendations.

The Committee expects that the industry will establish a pooling mechanism that is fair in its transfer of risks. Nevertheless, the Committee continues to be concerned about the possibility of unacceptable growth in the size of the residual market.

The Committee regards “creaming” of the market for preferred risks and the rejection of poor risks as an unfavourable business practice in the context of compulsory insurance. The Committee is concerned about the manner in which an insured is classified as a residual risk and about the “population” of drivers transferred to the Facility in recent years. Some details concerning the present population were provided to the Committee and are set out in Appendix G.

Accordingly, the Committee strongly encourages the industry to set up guidelines regarding who should be classified as a residual risk. Furthermore, **the Committee recommends** that the industry be required in legislation to inform the insured of the conditions for which he is being transferred to the residual market. The industry should also be obligated to inform the insured when such conditions have lapsed and be prepared at that time to offer him coverage as a regular customer. This requirement is unnecessary under a take-all-comers approach but is particularly important in the event that a residual market mechanism is established which channels the insured to a separate servicing carrier or establishes a separate rate for the residual risk.

CHAPTER 4

The Motor Vehicle Accident Claims Fund

No system of compulsory insurance will ever be perfect and there will always be some motor accidents caused by uninsured drivers. There will likely always continue to be accidents caused by hit-and-run drivers, uninsured out-of-province drivers, drivers operating vehicles without the owner's consent and unlicensed vehicles such as farm vehicles. Further, regardless of the system of compliance and enforcement that is established it is probable there will always be a few drivers of unlicensed, uninsured Ontario vehicles.

Since any of these uninsured drivers may be involved in accidents, the Committee recognizes that it is important that the Motor Vehicle Accident Claims Fund or an equivalent mechanism be maintained to pay the claims of victims, as required.

The Committee in its First Report had the opportunity of examining the ways in which the problem of the uninsured driver is handled in several other jurisdictions. Two alternative methods were:

- “In the United Kingdom, the industry has established its own Motor Insurance Bureau which pays uninsured driver claims and then bills its costs back to all of the automobile insurers in the country rateably”.¹ In Ontario a similar approach could be taken either separately or in conjunction with the Facility.
- “In Switzerland, the government regulatory authority arranges for an automobile insurance company to handle all uninsured driver problems and pays a premium to the company for doing so. This premium is then charged back against all automobile insurance companies rateably.”² The Committee is attracted to this alternative but recognizes that a number of years of experience under the compulsory insurance system might be required before it would be possible to determine the extent of the uninsured driver problem to be assumed by the servicing carrier.

A third alternative might be no Fund; instead, uninsured motorist coverage would be offered to the consumer. The Committee finds this alternative unacceptable.

While other methods of handling the uninsured driver may be considered in the future after implementation of compulsory insurance, **the Committee recommends** that, at present, the Motor Vehicle Accident Claims Fund be maintained. At the same time, **the Committee recommends** that

1. Select Committee Company Law, *First Report on Automobile Insurance*, page 180.

2. Ibid.

the Motor Vehicle Accident Claims Act be amended to ensure that innocent victims will be compensated to the full extent provided for under all forms of compulsory insurance, including Accident Benefits coverage.

The remainder of this section examines the ability of the M.V.A.C.F. to meet its expected payments under a compulsory insurance system.

In the past the receipts of the M.V.A.C.F. have come from four sources:

1. Uninsured motorists' vehicle fees of \$100 received from each vehicle owner who decides to pay into the Fund in lieu of purchasing third-party liability insurance.
2. A portion of each driver's licence fee, that is, \$1 of the fee paid by each driver for his licence is paid to the Fund each year.
3. Interest on the investment of the Fund's balances.
4. Reimbursement by uninsured motorists of claims paid to accident victims.

Payments by the Fund have been for:

1. The settlement of claims, including not only payments directly to the claimants, but also payments of legal and other costs involved in resolving claims.
2. The expenses of administering the Fund.

Over the years the Fund has built up a considerable surplus as receipts have exceeded payments. A summary statement of the operations of the Fund for the year ended March 31, 1977 is as follows:

MOTOR VEHICLE ACCIDENT CLAIMS FUND
STATEMENT OF OPERATIONS
YEAR ENDED MARCH 31, 1977
 (000's omitted)

Receipts		
Uninsured motor vehicle fees		\$ 7,979
Driver's fees		4,078
Interest income		2,481
Repayments by debtors		2,454
		<u>\$16,992</u>
Payments		
Claim cases	\$2,666	
Judgement cases	9,399	
Hit-and-run cases	1,869	
Administration costs	2,868	16,802
		<u>16,802</u>
Excess of receipts over payments		\$ 190
Balance of Fund—March 31, 1976		31,913
Balance of Fund—March 31, 1977		<u>\$32,103</u>

Payments from the Fund for “cases” are the cash payments made in the year in full or partial settlement of claims. No provision is made in the annual statement for future payments for claims that remain open or for claims relating to accidents that may have occurred but have not yet been reported.

Approximately 47% of the receipts of the Fund in 1977 were from uninsured motor vehicle fees, which will be eliminated with the implementation of compulsory insurance. In addition, the Fund will no longer earn interest income on the average funds it is presently able to invest from this source. Currently this income would be in the order of \$300,000 annually. On the other hand, it has been estimated by Ministry staff that, with the implementation of compulsory insurance, the total payments from the M.V.A.C.F. would decline by 50% after pending claims are settled. If these estimates are correct, a pro forma statement of the Fund for a future year based on 1977 operating information might show:

Total receipts	\$8,713,000
Total payments	<u>8,401,000</u>
Excess of receipts over payments	<u>\$ 312,000</u>

The Fund had in excess of \$32 million at March 31, 1977 and it appears it will not require any additional revenue to finance its current operations. However, M.V.A.C.F. officials have recently undertaken a programme to set up reserves for future payments and have informed the Committee that \$15 to \$16 million of the \$32 million balance in the Fund has already been allocated by working through approximately half of the claim files. The Committee has also been informed that the M.V.A.C.F. has accounts receivable of about \$30 million from the uninsured drivers on whose behalf claims were paid. M.V.A.C.F. officials expect that about one-third of current accounts receivable and the same proportion of future claim payments will be recovered by the Fund.

The impact of the above factors cannot be fully determined. In addition, other considerations make a positive statement concerning the precise status of the Fund impossible at this time. For example, the full impact of the increase in the minimum coverage from \$50,000 to \$100,000 as at January 1, 1977 is still a matter of conjecture, and the future investment income the Fund is likely to earn is difficult to determine. Nevertheless, it appears to the Committee that payments on claims under a compulsory insurance system would likely have to be funded by new revenues and could not rely on the current outstanding balance in the Fund.

The major source of income to the Fund in future, if no change is made to the present system, will be from a portion of the drivers' licence fees. This fee, which is levied on *all* drivers, spreads the losses from unin-

sured drivers to all licenced drivers. If any excess of payments over receipts should occur in the future, **the Committee suggests** that the deficiency could be financed initially from any surplus cash on hand and then in several alternative ways, including among others:

- increasing drivers' licence fees
- retaining the drivers' licence fees as at present and collecting "premiums" from all insurers in the Province on a pro rata basis
- using general revenues of the Province to offset a portion of the cost
- using revenues from the existing or an additional gasoline tax to reflect all or a part of the required revenues.

If any alternatives to the present system are chosen to finance all or a portion of the "excess" costs of the Fund, the underlying principles of loss distribution among the drivers of the Province, the vehicle owners in the Province, and the public at large must be faced.

PART II

AUTOMOBILE ACCIDENT COMPENSATION

CHAPTER 5

No-Fault Automobile Accident Compensation

A. INTRODUCTION

In its First Report, the Committee reviewed in detail the philosophical debate about the no-fault concept of automobile accident compensation. It then pointed out that Ontario, like other Canadian jurisdictions, had taken a first step in the direction of adopting the no-fault philosophy when it adopted Accident Benefits coverage in 1972. The Committee indicated that it intended to make more thorough investigations of this concept before formulating any final recommendations and it recommended, that in the meantime, the existing Accident Benefits coverage should be enriched substantially. Since the publication of the First Report, regulations have been enacted, as set out in Appendix H, enriching the Accident Benefits coverage in accordance with the Committee's recommendations. The Committee has now had the opportunity of completing its more detailed investigations and of formulating its conclusions about the no-fault concept.

In particular, the Committee's consultants have provided the Committee with a comprehensive report on their studies of the no-fault concept and the Committee includes this information as Background Study One on "Automobile Accident Compensation: The No-Fault Approach".

In addition to its study of the consultant's report, the Committee has heard in detail from representatives of the industry and the agency system in Michigan, a state with the most advanced and far-reaching no-fault system in the United States, one which has been in operation since October 1973. It has also held sittings in Boston, Massachusetts, where the longest established no-fault system in the United States has been in effect since January 1971. The Committee has also travelled to Washington, D.C. to confer with senior representatives of the U.S. Senates' Committee on Commerce, Science and Transportation which has conducted extensive studies of no-fault systems and has been studying bills that would lead to the creation of a federal standard for no-fault systems for the entire United States. Studies in Dade County, Florida, where a no-fault system has been in effect since January 1972, were especially helpful because that jurisdiction has experienced an assortment of automobile insurance problems, including those related to their no-fault system, and has been particularly aggressive in experimenting with solutions. In addition, the Committee has reviewed the Quebec legislation for a no-fault bodily injury compensation system that came into effect on March 1, 1978. It has furthermore had an opportunity to study the details of Variplan, a modified no-fault plan prepared by the Insurance Bureau of Canada in 1974.

This chapter contains a brief statement outlining the present system in Ontario and the alternative of a pure no-fault system. The next two

chapters follow with some of the Committee's considerations in evaluating the no-fault concept in relation to bodily injury claims and to own-vehicle damage claims. Chapter 8 provides the Committee's conclusions and recommendations on the subject of a no-fault programme. Substantial additional detail is set out in Background Study One on "Automobile Accident Compensation: The No-Fault Approach" which begins at page 263 of this report.

B. THE PRESENT SYSTEM IN ONTARIO

The present system of automobile accident compensation in Ontario is based on the common law principle that the driver or owner of an automobile is responsible for injury or damage resulting from an accident to the extent, and only to the extent, that the driver was negligent. Conversely, the victim is entitled to compensation only to the extent that his own conduct was free of negligence. As a result, questions of compensation tend to be dealt with in an adversary atmosphere and disputes over liability are settled through a process of adjusters and, when necessary, of courts and lawyers.

Integrated with the operation of the common law principle is a system of third-party liability insurance, whereby the loss that the insured would otherwise have to pay can be lifted from the insured's shoulders and distributed throughout the entire automobile insurance system. The result of this integration is that the effects of the common law rule of responsibility for negligence are minimized.

There are two exceptions to this general pattern of compensating third parties. The first involves the system of Accident Benefits coverage which the Ontario Legislature established in 1972. This is a mandatory adjunct to third-party liability coverage which provides for the payment of certain limited benefits in the event of bodily injury or death, regardless of any question of fault. Despite the establishment of this coverage, the vast bulk of the payments for bodily injury compensation are still being made under third-party liability coverage and the "fault" system. The other exception is the long-established system of collision and comprehensive coverage, whereby the insurer pays its own insured's vehicle damages, subject to the pre-agreed deductibility amount, entirely irrespective of fault or innocence. In both cases insurance companies have the right to recover that portion of their payments which can be assigned to the fault of another party. This right is waived in the case of Accident Benefits but, in the case of collision claims, reimbursement through subrogation against the party at fault or his insurer is pursued by insurers as a matter of routine.

Despite these two exceptions, the general pattern of the present system involves payment of compensation to victims to the extent that they are innocent, through the medium of third-party claims against an insurer.

C. THE ALTERNATIVE OF NO-FAULT

The Committee is currently faced with the opportunity to comment on no-fault automobile insurance as a fundamentally different method of compensation that establishes for all insureds a first-party mode of recovery for losses and takes away the right of an injured party to sue a driver for recovery of damages. In this way, it establishes the right of all persons suffering losses in an automobile accident to recover an appropriate measure of their damages without the need to prove negligence on the part of another driver.

The emphasis of this approach to compensation for bodily injury is similar to that on which health insurance or workmen's compensation insurance is based in Ontario. In brief, a *pure* no-fault automobile insurance system covering *bodily injury* would require a law specifying the following:

- "An injured person would request compensation only from his or her own insurance company (first-party basis). He or she would *not be allowed to sue* anyone else for this purpose. Negligence, or fault, would be irrelevant.
- No-fault insurance would be compulsory, and all auto-insurers would be required to provide it, without the option of cancelling.
- The no-fault insurance would cover only economic losses due to injuries or fatalities—medical expenses, loss of income and expenses for substitute service.
- Since pain and suffering cannot be measured in dollars, these losses would not be covered.
- To minimize costs, duplicate payments for the same loss would be prohibited."¹

In addition provision should also be made for the following factor:

- Compensation would be provided to all occupants of the vehicle, pedestrians and any person injured by the insured vehicle. Provision would also be made for compensation to persons injured by uninsured or unidentified vehicles.

In the *property damage* area, no-fault coverage for own-vehicle damage is similar in approach to the collision coverage currently purchased by about three-quarters of Ontario passenger vehicle owners. The payment of losses is made directly by the insurer to its own insured entirely irrespective of fault or innocence. However, under no-fault, if the vehicle owner is not insured against damage, he cannot sue anyone else for recovery and therefore must bear his own loss. In addition, a no-fault system for vehicle

1. *Consumer Reports*, "Managing Your Auto Insurance", August 1977, page 487.

damage differs from collision coverage in that the insurer cannot subrogate from the insurer of the party at fault for reimbursement of payments made to his policyholder. As a result all claims settlements are handled strictly on a first-party basis.

CHAPTER 6

Advantages and Disadvantages of the No-Fault Concept

The Committee's consideration of the no-fault concept centred around the following basic issues:

1. The concept of universal entitlement to compensation versus recovery by the innocent victim;
2. The extent of compensation that can be provided under a typical no-fault system in comparison to recovery under the tort system;
3. Differences in the methods and efficiency of payment under the two systems; and
4. The concept of punishment of negligent conduct.

A discussion of these factors follows, with emphasis on compensation for bodily injury.

A. COMPENSATION FOR ALL VICTIMS

No-fault bodily injury systems are propounded with a view to achieving certain social goals. They seek to provide compensation for *all* victims for some realistic measure of losses arising out of bodily injuries incurred in automobile accidents, on the ground that *the plight of accident victims is a matter of social concern*, regardless of who can be said to be at fault. In comparison, the chief priority of the fault liability system of compensation is to protect the innocent victim of negligence by providing a means of recovery of losses from the party at fault in an accident.

The Province of Ontario has already adopted the principle that every person injured in an automobile accident should expect to be compensated to the amounts provided under Accident Benefits coverage and therefore should be assured that he will not be forced to bear his loss solely on his own. The Committee is currently concerned with deciding whether the no-fault concept should serve, not as a supplementary coverage, but as the *fundamental* basis for granting compensation to victims of motor vehicle accidents.

In this regard, it is sometimes argued that a driver will be willing to pay more in premiums for a small measure of added protection on a no-fault basis, as long as the right to tort action is retained for full recovery from the blameworthy driver. The Committee is concerned, however, that this approach may not ensure that the needs of all persons injured on the roads are adequately provided for, since an affordable no-fault coverage on this basis is likely to provide universal benefits that are too low for the majority of the injured population. In particular, the Committee is concerned that the needs of the families of at-fault or partially at-fault drivers may not

be adequately covered under such a scheme of no-fault benefits. Before making its recommendation in this matter, the Committee considered further arguments in the no-fault debate as discussed below.

B. EXTENT OF COMPENSATION

A no-fault system guarantees to every injured person the right and the means to recover a reasonable measure of his or her loss without regard to fault. However, it is argued that a no-fault programme may undercompensate innocent victims in order to give some compensation to all victims.

The Committee recognizes that, if the no-fault system is to serve as an effective substitute for tort recovery, a generous and equitable system of compensation must be established on a no-fault basis. It is, however, readily apparent that a typical no-fault system will likely not compensate the injured person to the full extent provided under the tort system in at least two categories of loss: the amount designated as a weekly indemnity to replace wage loss and the amount, if any, to be paid for non-economic loss.

The Committee comments below on these and other benefits which would typically be paid under a no-fault plan for both economic and non-economic loss resulting from bodily injury. While there is a broad variation in the terms of no-fault automobile insurance policies from one system to another, the following describe the more common variants.

Economic Loss

- (a) All reasonable medical expenses, and all proper expenses related to physical rehabilitation. Typically, these expenses are paid without any limitation on the amount.
- (b) Compensation for lost earnings. An analysis of various pure no-fault systems indicates the following variants:
 - Normally payments continue for an unlimited time and have no limit on their aggregate amount.
 - Frequently there is an absolute maximum on the weekly sum payable. This maximum can be set at an amount that would cover the weekly wage losses of the bulk of the population, say the lower 85 percent of the population. This provision avoids having many low-income premium payors contribute excessively so as to provide high compensation payments to those few who have unusually high incomes. For the latter, additional disability income coverage can be made available on an optional basis, either as a supplement to the automobile policy or as a separate policy sold by traditional disability income insurance carriers.
 - A no-fault system may carry a further rider whereby only a portion of income losses are paid. This provision is said to make some allowance for saved income tax and to encourage prompt recovery.

- The victim who is a non-earner at the time of injury may nevertheless incur loss of potential earnings, as in the case of students or unemployed persons. In such cases a no-fault system can provide for the calculation of earnings with due allowance being made for the time when such a person would have secured employment, if the accident had not occurred.
 - A similar problem is that of the non wage-earning spouse who may not literally suffer a loss of income, but who nevertheless ceases to be able to keep house or care for the children. In such cases, replacement expenses are sometimes provided to pay for temporary help.
 - Partial loss of income as a result of partial disability is a complicating factor that is treated in a variety of ways. Generally, however, no-fault systems provide for payment of income in excess of *actual* earnings during the period of partial disability, up to a weekly maximum.
- (c) Certain out-of-pocket expenses such as those for special care, technical assistance, prosthetic equipment, drugs, damaged clothing or personal effects and miscellaneous disbursements resulting from the accident are included.
- (d) Death benefits are normally paid under pure no-fault systems on the basis of actual loss as contrasted with the alternative fixed sum approach on which Ontario's Accident Benefits coverage is based. Under the latter scheme insurers are required to pay fixed benefits to surviving family members on the basis of a scale of payments related to family size. This scheme does not relate payments to actual losses; rather, actual losses are deferred for such disposition as they may receive under the third-party liability fault system. In contrast, payments under no-fault systems are usually based on the dependants' out-of-pocket expenses, such as funeral costs, plus their *actual* loss of supporting income which is payable on an instalment basis up to the established weekly maximum.

In general, the Committee finds that a no-fault system can be structured in such a way as to provide adequate and comprehensive coverage for economic losses. For example, all medical, rehabilitation and out-of-pocket expenses are typically reimbursed without limit on their amount. In addition, payments are made to cover some reasonable level of earnings-related losses, including losses of supporting income in the event of death of the household head or principal family wage-earner.

In the matter of wage loss coverage, the Committee views a no-fault policy, which would provide for the reimbursement of lost income without any monetary limit, to be inequitable and unacceptable as a compensation approach since it obligates all motorists to share in the costs of reimbursing the high income earner injured in an accident. Accordingly, it is more rea-

sonable, in the Committee's opinion, to set a generous but realistic maximum weekly limit on the amount of wage loss benefits payable under the compulsory policy. Wealthier individuals, desiring full earnings-related benefits, are expected to be able to afford the purchase of additional wage-loss coverage.

Problems, however, arise under a no-fault system in structuring benefits payable to partially disabled workers, and to non-earners, such as students, the unemployed and non wage-earning spouses. Losses suffered by these persons are not readily defined in as precise a manner as lost income calculated on the basis of earnings prior to the accident. Standard guidelines in a no-fault programme for compensating persons in these circumstances may not be as flexible as a case-by-case evaluation of circumstances under the fault-liability system.

Non-Economic Loss

The tendency of a no-fault system to place limited value or even no value on non-economic loss is a major factor in the argument that a no-fault system undercompensates innocent victims. *Pure* no-fault systems limit compensation exclusively to economic losses, which is to say to those that can be directly measured in dollars.

The argument for eliminating non-economic loss payments under a pure no-fault system is twofold. Firstly, it is argued that non-economic loss cannot be objectively and consistently evaluated and hence cannot be directly measured in dollars. Payment of such a loss would therefore appear to violate the no-fault principles of objectivity and equity. A second argument states that there is inevitably a limit to the amount of money available for the payment of compensation and that it is more important that such money be available to pay the *economic losses of all victims* regardless of fault.

Those who would eliminate the payment of damages for such losses as pain and suffering also state that, in practice, the bulk of such damages are paid to settle relatively minor injury cases and that these payments tend to overcompensate those who suffer minor injuries.¹ It is further said that, in cases of very grave personal injury, payments for pain and suffering tend to be low relative to the severity of the injury and the size of the award for economic loss.

On the other hand, there are many who accept the no-fault concept in

1. This inequity arises from the fact that the industry sometimes finds it less expensive to over-pay small claims than to process them through the courts. The Committee had a personal opportunity of observing the dangers inherent in such a policy when it conducted investigations of automobile insurance practices in Dade County, Florida. There, such a policy of appeasement in relatively minor cases had resulted in such an escalation of claims costs, that prevailing premiums in that rating territory have become almost unaffordable.

general but insist that non-economic losses should continue to be recognized as a legitimate basis for damages. They join with proponents of the common law liability system in saying that pain and suffering may not be visible, but it is certainly no less real. The fact that the dollar amount payable may be more difficult to calculate than the amount of lost wages is discounted as a problem by the fact that skilled judges and lawyers have developed a broad experience and a refined judgement for determining what constitutes fair compensation in each individual case.¹ Finally, advocates of the fault system say that it is fundamentally wrong to abolish or even to reduce the payment of compensation for pain and suffering to innocent victims so that payments can be made to the careless and the guilty.

Taking into account the above arguments, some no-fault systems establish a fixed scale of benefits for non-economic loss to be paid in a lump sum, the amount of which varies by type of injury. Generally these lump sum amounts are nominal and correspond only to pre-determined, readily observable physical injuries. Other "modified" no-fault systems allow a victim to sue for the full measure of non-economic losses in accordance with the accepted rules of the fault system, if his injuries are serious. Tests of seriousness, called "threshold tests", have been introduced in other jurisdictions and include the duration of disability, the amount of the medical expenses incurred, and the gravity or permanence of the injury. These are referred to as "time", "dollar" or "verbal" thresholds respectively. The effectiveness of these thresholds in limiting tort recovery of non-economic loss to cases of serious injury is largely determined by the objectivity and nature of the conditions specified in the wording of the threshold. Experience in U.S. jurisdictions appears to indicate that a "verbal" threshold, properly designed, is the most effective in discouraging overutilization of the tort recovery system.

The Committee recognizes that the arguments on both sides of the debate regarding non-economic losses are matters of judgement. It also recognizes that, if a no-fault system is to accommodate payments for pain and suffering and other non-economic losses, it can only do so by way of arbitrary nominal payments. Unspecified allowances for non-economic loss payments on a first-party basis would re-introduce an adversary situation between the insurer and his own insured in determining the appropriate amount of such payments. Accordingly, any decision to retain the payment of full damages for non-economic loss would seem to be best accommodated under the tort recovery system.

1. Three recent decisions of the Supreme Court of Canada would seem to suggest that \$100,000 serve as the maximum to be awarded for the present for damages for pain and suffering. See *Thornton vs. S. Dist. No. 57 Bd. of S. Trustees*, (1978) 1 W.W.R. 607 (S.C.C.); *Andrews vs. Grand & Toy Alta. Ltd.*, (1978) 1 W.W.R. 577 (S.C.C.); *Arnold vs. Teno*, (1974) 7 O.R. (2d) 276; 11 O.R. (2d) 585; S.C.C., January 19, 1978.

Cost Considerations Related to the Level of No-Fault Benefits

Introduction of no-fault compensation is unlikely to effect a reduction in total automobile insurance costs. Because the number of persons to be compensated is increased, the amount of compensation payable to each must be limited in some way, otherwise the cost of the insurance system could exceed tolerable limits.

A detailed costing study of a no-fault plan is not feasible until the plan is fully formulated and appropriate data, not currently assembled by insurers, is collected. However, in the course of its investigations, the Committee has identified certain important considerations that have a bearing on the question of cost.

1. Any "add-on" approach to no-fault, which expands first-party benefits, without any restriction on tort recovery of excess or residual losses, runs into funding problems. Increased premiums are necessary to extend compensation for economic loss to more injured persons, without limiting the right of innocent victims to collect, in full, both their economic and non-economic losses. Such is the case when a programme of enriching Accident Benefits coverage is undertaken.
2. There is a significant saving to be achieved from placing limits or restrictions upon the payment of damages for non-economic losses, particularly in the many relatively minor instances that constitute the vast bulk of bodily injury claims.
3. A no-fault system which eliminates tort recovery of non-economic losses or effectively restricts such recovery to cases of severe injury can release substantial funds for first-party economic loss benefits. Accordingly, a no-fault system does not necessarily result in any significant increase in total costs, as demonstrated by the introduction of the modified no-fault system in Michigan.
4. In designing a no-fault system of compensation it is possible to "fine tune" the exact benefits to be paid so that they will be consistent with affordability. For example, wage loss benefits can be paid to a maximum weekly limit consistent with an affordable premium level for the no-fault insurance policy.
5. Offsetting in some part the higher benefit costs possible under a no-fault plan, are savings to be derived from the elimination of fault investigation and from the greater efficiency of a first-party claims settlement process. A general discussion of these matters follows in the next section.

The Committee concludes from the above factors that a no-fault programme can be formulated which can compensate the average injured person for substantially the full extent of his economic losses without effecting any significant increase in total automobile insurance costs. This conclusion

is, however, conditional on the significant limitation of payment of damages for non-economic loss.

C. METHODS OF PAYMENT

One of the objectives of a no-fault system is to provide the injured person with the certainty that he will be compensated, and with certainty as to the amount he will receive. Following from this objective is another, that of providing prompt and efficient payment of claims.

It is the Committee's view that the tort system of compensation which has developed within common law has in fact served the residents of Ontario well in comparison to less efficient and sometimes abused tort systems in some other jurisdictions. For example, many of the abuses and high costs of the tort system which led to adoption of no-fault features in the U.S. are not evident or not as serious in Ontario: the extent of litigation, delay in the courts, the amount of legal fees, and the trend towards soaring costs of court awards for bodily injury are in general of less concern in this Province than in the United States. Nevertheless the Committee is convinced that improvements are necessary in Ontario to provide better protection to the injured person, greater efficiency in the claims settlement process and improved convenience to the claimant.

In this regard the Committee has considered two alternatives: reforms under the fault or adversary system of third-party settlements; or adoption of a no-fault programme of first-party settlements. In other Parts of this Report the Committee comments on its suggestions for improvements in the third-party settlement process. The following suggestions can be added as additional ways of improving the present system:¹

- Adoption of a compulsory unlimited liability policy (as previously proposed by the Committee);
- Increased use of advance payments under Section 223 of the Insurance Act;
- Enactment of legislation requiring insurers who are disputing the basis on which they must share responsibility for Accident Benefits payments to pay the victim equally and without delay, leaving the issue between them to be sorted out later;
- Establishment of more stringent rules to speed up the operation of the judicial process, including the use of pre-trial proceedings;
- Elimination of the defence of inevitable accident;
- Reform of the format of jury verdicts;
- More rigorous treatment of insurance fraud.

1. Submissions of the Insurance Committee of the Advocates Society with respect to No-fault Insurance, February 4, 1975.

However, no-fault supporters reply that these measures do not solve the problems that are peculiar to the present fault system in that they ignore the need to provide compensation to *all* victims with economic losses. They also point out that these suggestions ignore the savings that result from the elimination of fault from the claims process and from the establishment of the claims process on a first-party, or "insured-to-his-insurer" basis.

In contrast, under the alternative of a no-fault programme the following advantages are said to exist:

1. *Avoiding the Difficulty of Proving Fault*

The present fault liability system of compensation is intended to protect the innocent victim of the motor vehicle system. However, the need to prove negligence is said to present certain hazards even to the innocent: the delay in the start of investigative procedures may confuse the reconstruction of events; speed and traffic congestion may confuse observers; delays in reaching trial may dim the memory; and witnesses may prove unavailable or unreliable.¹ It is argued that these hazards can easily result in injustice being done even to the innocent persons whom the fault system is designed to protect.

In contrast, since there is no need to prove negligence under no-fault systems, such hazards are avoided.

2. *Promptness of Recovery Under No-Fault*

In addition to the uncertainty associated with determining liability is the delay that is involved in a fault system, particularly when claims go to court. Critics of the present fault system say that this delay can hinder physical recovery, increase inconvenience, set back rehabilitations and instil a feeling of grievance.

In contrast, a no-fault system dispenses with disputes about fault and enables instalment payments to be started promptly, with direct payments made by the insurer to its own policyholder.

3. *Saving Recovery Costs*

The high cost of recovery under the present fault system is another source of dissatisfaction. Laborious claim settling processes and associated legal expenses result in increased adjusting costs for insurers and these inevitably are passed on to the public in increased premiums.

Claimants are likely to find that they too must bear additional legal expenses since even the contribution of the insurer to the successful claim-

1. Select Committee on Company Law, *First Report on Automobile Insurance*, page 67.

ants' total legal expenses—generally considered to total about 15 percent of the amount of the recovery,—may be insufficient to cover total charges for legal services rendered. Such legal costs are eliminated in a pure no-fault system.

4. *Efficiency of Operation*

In general, a pure no-fault bodily injury system is said to perform with a high level of efficiency. More specifically, it is contended that:

- Payments are made more promptly;
- Payment procedures are simpler and more readily understood both by industry employees and by the public as well;
- Flexibility is built into the system, so as to meet such circumstances as changing rehabilitation needs or changes in the cost of living;
- Duplication of compensation payments can be eliminated. No-fault automobile insurance is generally made the first payor of compensation for automobile accidents, so that the losses from injuries arising out of the motor vehicle system are distributed across the entire vehicle-owning community. Other compensation schemes, such as disability policies, would then be required to adjust premiums to the extent that the first payor role of the automobile insurance system absolves other payors from liability. In the case of governmentally supported compensation plans such as health insurance, a simple and inexpensive method of reimbursement out of the automobile insurance system might be established¹ to provide reimbursement irrespective of fault;
- The expenses of claims settlement are minimized. A primary goal of no-fault systems is to return more of the premium dollar to the insured. In part, this is accomplished by the elimination of liability investigations and disputes with third parties.

5. *Periodic Payments*

Under the traditional fault system, compensation is evaluated at a specific point in time. Past damages are calculated and future damages are predicted, and then one lump-sum figure is fixed as the amount of compensation to be paid. This assessment is final and, after it is determined, it cannot be revised either upward or downward to reflect changing circumstances.

Contenders for the adoption of a no-fault system say that this requirement is entirely inappropriate to a fully effective compensation system. It is argued that it is impossible to make exact predictions at a point in time

1. Select Committee on Company Law, *First Report on Automobile Insurance*, pages 153-156.

about future earnings losses, medical conditions, life spans or other contingencies. Furthermore, since the lump sum paid under the present system can never be increased once its amount is determined, there is a real incentive to defer any settlement, and hence any payment, as long as possible, so as to make certain that all conceivable consequences of the accident are known and allowed for and perhaps even to emphasize the extent of injury. The expectation of a large lump sum award at the end of the process may make such a deferral tolerable. Lastly, it is argued that the fixed-sum award may result in windfall gains to persons other than the victim, as where a victim dies shortly after receiving a large payment and the award is passed on to others.

Under no-fault bodily injury systems, periodic payments are made to the victim as needs arise. And conversely, payments can be reduced as circumstances improve.

6. *Accountability*

In a fault-based liability system of compensation, insurers pay claims on behalf of their policyholders to another party. The policyholder is seldom concerned about the efficiency of his insurer in controlling costs and in reimbursing a third party.

Supporters of a no-fault system argue that a first-party settlement process under a no-fault plan encourages control of claims costs by insurers, particularly when insurers are unable to recover payments from the party at fault. In addition, in a first-party system, the insured driver is able to assess both the price and the service offered by his insurer, and is able to purchase with both these factors in mind.

The Committee has been unable to identify in monetary terms the full extent of efficiencies that might be achieved through adoption of a no-fault programme in lieu of the present mixed system of Accident Benefits coverage and tort recovery. Sufficient data on legal and adjusting costs in the present system to make a detailed calculation are not available. Nevertheless the Committee is convinced that savings will be forthcoming through elimination of the fault investigative process.

The Committee is, however, equally impressed with the opportunity presented by the no-fault system to establish a first-party settlement process that provides for direct accountability of the insurer to his own policyholder in the matter of claims, and, also, to make possible the payment of present and future damages on a periodic or instalment basis. Both these factors would contribute to the promptness of payments and to emphasis on compensation rather than on retribution.

D. THE PUNISHMENT OF NEGLIGENT CONDUCT

A recurring argument in support of the existing fault-based system is

that it promotes individual responsibility, while a no-fault system treats innocence and guilt alike and thereby dilutes individual responsibility. Some supporters of the present system consider that, for this reason, its retention is essential.

However, those who support no-fault say that, in practice, the present automobile insurance system has already virtually eliminated the negligent driver's obligation to pay for the consequences of his negligence, since about 90 percent of Ontario drivers under the present system know that the bulk of any damage they cause will be paid for out of their insurers' pockets and not out of their own. They add that the real sources of punishment under our present system are the criminal law, the licence suspension system, the anguish of involvement in an accident and the prospect of one's own death or injury as a result of careless driving. These deterrents are said to be as effective under a no-fault system as they are under the present fault system. The Committee also agrees that the real deterrents to careless driving fall outside the automobile insurance system and the common law system of liability.

CHAPTER 7

Own-Vehicle Damage

A. INTRODUCTION

The application of the no-fault concept to property damage is a matter which can be separated from consideration of the no-fault principle in relation to bodily injury. It is not necessary to guarantee to each and every vehicle owner the certainty that his vehicle damage losses will be met to the same extent that this certainty is required for bodily injury losses. At the present time the guarantee of recovery is extended only to those persons who can prove that their vehicle was damaged through the negligence of another person.

In contrast to bodily injury which is considered to be a matter of social concern, it is argued that the vehicle owner must be prepared to protect his investment in the value of his automobile on an individual basis. However, the vehicle owner is cautioned against too great a reliance on the tort system of recovery because:

“the speed and complexity of modern driving conditions often make it a meaningless exercise to assess fault or blameworthiness among the participants in an accident”.¹

A majority of vehicle owners in this Province, in the order of seventy-five percent, already purchase first-party collision coverage to ensure recovery of losses regardless of fault.

In considering the no-fault concept in relation to own-vehicle damage, the Committee directed its focus to the following two matters: the benefits to be achieved from an integrated no-fault insurance system of bodily injury and property damage coverage that completely eliminates fault investigation; and the opportunity for improvements to the current claims settlement process that may be forthcoming under a no-fault system.

In reviewing these matters, the Committee referred to experience in the states of Massachusetts and Michigan, the former state having abandoned its no-fault property damage legislation in 1976, and the latter state having entered into its fifth year under an integrated no-fault bodily injury and property damage system. An overview of the basic features of a no-fault own-vehicle damage system, as demonstrated by these two jurisdictions and proposed elsewhere, follows in this chapter.

B. SAVINGS IN NO-FAULT OWN-VEHICLE DAMAGE SYSTEMS

Those who support no-fault own-vehicle damage compensation main-

1. Select Committee on Company Law, *First Report on Automobile Insurance*, page 66.

tain that it effects a saving of cost. There are several ways in which such a system is said to accomplish this:

1. With no-fault own-vehicle damage coverage, the vehicle owner needs only to have his vehicle appraised in order to settle his claim with his own insurer. Questions of liability no longer need to be resolved and, as a result, substantial investigating expense and claims processing time is saved.

The present fault system may provide similar savings if the insured has collision coverage and his innocence in the accident is obvious. In questionable cases, however, there is normally a money-wasting and time-consuming dispute between the insured on the one hand and his insurer and/or the third party's insurer on the other hand, regarding the fault element in the accident. There may also be some dispute between the insurers themselves as to the sharing of responsibility. Even when inter-company arguments are resolved by the use of collision assessment charts, there is still an element of cost involved in working out the settlement.

Furthermore, the claimant who pursued his own claim, either for the full amount of damage if he has no collision coverage or for the deductible amount if he is covered on a first-party basis, is often frustrated and inconvenienced under the present system. In a no-fault system, all claims are handled by his own insurer.

2. Some legal expense is also saved under a no-fault own-vehicle damage system. The amount of such savings is not, however, as substantial as the savings available in the bodily injury area, since lawyers are much less frequently involved in cases that involve vehicle damage only. On the other hand, there is a regular resort to the small claims courts under the present system, as claimants seek to collect deductibles or to disprove liability in order to escape higher premiums. A no-fault own-vehicle damage system would eliminate or minimize this burden on the courts.
3. Since, under a no-fault own-vehicle damage system, insurers pay only for the damage done to their own insureds' vehicles, there tends to be greater emphasis upon tailoring the premium more precisely to the probable repair costs of each insured's vehicle. Experience has also indicated that there is some greater diligence on the part of insurers in minimizing repair costs when such costs cannot be recouped from another insurer by virtue of the principle of subrogation.

In Ontario about 60 percent of all compensation under the present system arises from vehicle damage. And correspondingly, the major part of the premium dollar is paid to cover vehicle damage. In the Committee's opinion, it is as important to save costs in the vehicle damage area as in the field of bodily injury. Opportunities for savings should be developed in the prop-

erty and vehicle damage area in order to free automobile insurance funds for more beneficial uses, including improvements in bodily injury benefits. Anything that the adoption of a no-fault system can do in this regard must be seriously considered since overall savings in the automobile insurance industry are an objective.

C. COST AND COVERAGE CONSIDERATIONS

While potentially effective in terms of the claims settlement process, the no-fault solution to vehicle damage coverage may still not be desirable. For example, the application of the no-fault concept to vehicle damage can create public dissatisfaction with respect to two related factors:

1. No-fault insurance means the driver must bear the cost of collision coverage for damage caused by another driver's fault.

Under the fault system, the costs associated with negligence can be shifted to the insurer of the party at fault through subrogation. The no-fault system eliminates the loss-shifting function so that no-fault own-vehicle damage insurance results in a redistribution of the premium burden. Under a fault system, drivers with at-fault claims records are charged proportionately more whereas, under a no-fault system, records of fault cease to exist. As a consequence, the current substantially higher premiums paid by careless drivers are replaced with slightly higher premiums for claims free drivers. This in turn results in a general levelling of premiums and an advantage to such groups as the under 25 drivers.

Experience in other jurisdictions indicates that it is nonetheless possible within the no-fault system to charge the careless driver with a greater share of the costs of insurance. For example, under the fault system in Massachusetts and in British Columbia, Saskatchewan and Manitoba, surcharges are applied consistently to all drivers with poor driver records on the basis of, among other factors, the number and type of driving convictions and traffic violations. Similar surcharges could be applied under a no-fault system.

2. Many vehicle owners may not want to bear the full cost of collision coverage; they expect to be compensated only in the event that they are not at fault.

This factor can be accommodated under a no-fault system with partial reliance on fault determination to allow purchase of limited collision coverage and deductible coverage. Recovery under these coverages from the first-party insurer would be based on the assignment of fault according to set rules of fault apportionment. However, insurers would not have the right to subrogate. To ensure that all vehicle owners are able to recover damages in obvious not-at-fault situations, limited collision coverage and/or deductible coverage could be made mandatory.

Limited collision coverage also has the advantage that it can be provided at a cost similar to that of the property damage portion of the present liability policy. In addition, a separate deductible policy made mandatory under a no-fault plan would mean that every vehicle owner would be sure to recover up to the standard deductible amount, to the extent that an accident was not his fault. Any vehicle owner wishing to protect his vehicle for recovery of damage in excess of the deductible could be allowed the choice of either no coverage, limited collision coverage in pre-determined blameless or shared-blame situations, or full collision coverage.

D. ABUSE OF THE NO-FAULT OWN-VEHICLE DAMAGE SYSTEM

Those who have observed the operation of no-fault own-vehicle damage systems say that their success can be endangered by abuse or overutilization. Simplifying the claims adjustment process makes it easier to take advantage of the insurance system, since it is easier to claim damage by a hit-and-run driver or allege that a third party caused an accident when there is no irate third party anxious to disagree. This has especially been the experience of Massachusetts, but it is nevertheless difficult to predict the extent of abuse, if any, that might develop under a no-fault own-vehicle damage system in Ontario. However solutions to the problem, if it arose, could include the threat of large fines in fraudulent cases and some increased use of fraud investigations, and these solutions might well be sufficient. A further possibility is the establishment of a rule requiring that an accident be reported promptly to the police as a pre-condition of entitlement to compensation. This might minimize the risk of fraudulent hit-and-run and stolen vehicle accident claims.

E. GENERAL OBSERVATIONS

It is generally argued that improved methods of claims settlement in the vehicle damage area can be achieved by extending the first-party settlement principle to vehicle damage claims under a no-fault system. An important advantage of a no-fault own-vehicle damage plan is said to be the elimination of the subrogation function, resulting in increased accountability of the insurer to his own insured and in elimination of costs of involving more than one insurer in the settlement process. Advocates of no-fault systems contend that appropriate alternatives can be made available under a no-fault own-vehicle damage plan which will tailor coverages and cost to the recovery expectations of the public. Finally it is argued that the integration of own-vehicle coverage with bodily injury coverage in a no-fault system will provide the best means of achieving savings in the automobile insurance system by completely eliminating the investigation of fault.

CHAPTER 8

No-Fault Automobile Accident Compensation: Conclusions and Recommendations

CONCLUSIONS AND RECOMMENDATIONS

The Committee has considered carefully the arguments that have been put forward with regard to no-fault compensation systems and it has examined the experience that other jurisdictions have had with them. It has also reviewed the reports received from its consultants and has studied other material, such as the 1973 Report of the Ontario Law Reform Commission on *Motor Vehicle Accident Compensation*.

The Committee has reached certain conclusions with regard to no-fault compensation systems and they are as follows:

1. In formulating its conclusions, the Committee began by addressing the basic issue: whether fault should continue to be the fundamental factor to be considered in determining whether compensation should be paid for motor accident losses. The Committee is particularly impressed with the capacity of no-fault systems to compensate *all* victims, regardless of fault, rather than paying only the relatively innocent. It is also impressed with the capacity of no-fault systems to reduce adjusting and settlement costs by minimizing fault investigation, so that a significantly larger portion of the premium dollar will be returned to the public in claims payments. **The Committee accordingly recommends** that "fault" should no longer be the fundamental factor to be considered in determining whether compensation should be paid for motor accident losses.
2. Having reached its conclusion in favour of the general no-fault principle, the Committee then considered the more specific area of compensation for bodily injury. It observed that the advantages of no-fault were even more compelling in this area than in any other. **The Committee has therefore concluded** that Ontario should establish a full no-fault programme of bodily injury compensation for economic loss and that the new programme should supersede the present Accident Benefits coverage.
3. Turning from questions of general principle to more specific matters, **the no-fault bodily injury programme which the Committee recommends for Ontario should include the following detailed characteristics:**
 - (a) The no-fault bodily injury compensation programme should define all the various economic losses for which compensation is to be paid and the limits (if any) to be imposed on each type of compensation. *All* victims should then be entitled to recover from their insurers (or from the Motor Vehicle Accident Claims Fund, if there is no insurer)

to the full extent provided for in the programme. The victim will neither need, nor be able to obtain, recovery from the other driver, or from the other driver's insurer.

- (b) Compensation for economic losses suffered should include:
 - (i) medical expenses without any monetary limit;
 - (ii) rehabilitation expenses without any monetary limit;
 - (iii) partial or total loss of income should be re-imbursed, subject to a reasonable weekly maximum amount. However, there should be no ceiling in the duration of payments, other than the time required to get back to work;
 - (iv) where there is no *literal* loss of monetary income, but there is nevertheless a loss of services such as necessary housekeeping or child care services that someone must be hired to provide, payment should be made to cover the actual cost incurred. Such compensation should be subject to a reasonable weekly maximum.
 - (v) death benefits should include any reasonable funeral cost and benefits payable to survivors in accordance with a scale of the sort that is now in effect for Accident Benefits coverage.
 - (vi) if the spouse or dependants have actually suffered a loss of support that exceeds the lump sum benefits provided for in (v), the excess should be paid to them in periodic payments that may be revised or terminated in the event of the recipient's death or remarriage or the expiration of the period during which the deceased would have provided support to such dependents. Such payments should be made subject to a reasonable weekly maximum amount.
- (c) The programme to be established should provide for the making of instalment payments in order to provide flexibility.
- (d) The Committee anticipates that its proposed no-fault programme will reduce disputes over compensation to a minimum,—certainly far below the present level. However, adequate provision should be made for the settlement of such disputes as may arise and so the present arbitration provisions of the standard policy should be retained, together with a full right of resort to the courts.
- (e) Compensation should be extended to provide for the needs of all persons suffering economic losses arising from a motor vehicle accident. In this regard the needs of the spouse and dependent children of the injured driver must be considered. Accordingly, compensation should not be denied to those injured persons who were involved at the time of the accident in the commission of a criminal offence such as escaping arrest or driving while their ability is impaired through the use of alcohol or drugs. The Committee has concluded that com-

pensation should cover such instances, so that economic losses arising from the motor vehicle system are borne within that system, rather than being borne by other systems such as O.H.I.P.

4. The Committee has been concerned with the arguments that it has heard with regard to the abolition of compensation for non-economic losses such as pain and suffering. Certainly there is a saving to be gained from the elimination of this area of compensation, and this saving is particularly tempting in view of the intangible character of such payments. It is equally significant that the elimination of such damages can end the high cost of fault investigations and adversary proceedings,—savings that are certainly important to the long-term health of any form of automobile insurance system.

And yet, despite the logic of these arguments, the Committee has concluded that it is wrong to eliminate all compensation for such non-economic losses. The Committee is convinced that these losses represent a legitimate class of loss which should not be disregarded if the objective of generous and realistic compensation for the complex damages resulting from bodily injury is to be met. The Committee believes that there is an expectation among the insured public of compensation for categories of loss such as pain and suffering, and that this expectation should not be denied, particularly in cases of serious injury.

The Committee is convinced that reasonable adjustments can be made in the no-fault programme which will enable some fair compensation for non-economic losses to be paid in appropriate cases without vitiating the basic concept. The conviction has been strengthened by what the Committee has learned about the operation of such modified systems in Massachusetts, Florida and Michigan. **The Committee therefore supports** the principle that there should be some provision within the proposed no-fault programme for compensation in bodily injury cases for non-economic losses.

5. **The Committee recommends** that its proposed no-fault programme include provision for payment of some compensation for non-economic losses by the insurer to the insured in some cases. Such compensation should take the form of a lump sum to be set out on a fixed scale which would provide an exact amount for each type of injury. The Committee has been interested in particular in the scale that has been established in New Zealand and is described in Table 7 of Appendix A to the Committee's Background Study One. The amounts should be modest, in keeping with the fact that they are payable to *all* victims regardless of fault and without the need for any evidence of the *actual* extent of the non-economic loss. Furthermore, the scale should allow for payments only where injuries are physically observable and medically certifiable.
6. The Committee recognizes that some cases of bodily injury may be so

serious that it would be unfair to limit non-economic compensation to that set out on a scale, in part because scale payments are inevitably only rough approximations and in part because they are necessarily modest in amount. In order to make a fairer provision for the most serious cases, **the Committee recommends** that a victim who has been injured in a motor accident should be entitled to recover compensation from a third party to the extent of his non-economic losses such as pain and suffering but only in the following circumstances:

- (a) He must be able to establish that he has suffered:
 - (i) serious and permanent injury resulting in substantial and medically demonstrable permanent impairment affecting the resumption of customary activities; or
 - (ii) permanent loss of important bodily function; or
 - (iii) significant permanent scarring or disfigurement;otherwise he is not to be entitled to make any claim whatever against any third party.
- (b) He must be able to establish at the very beginning of any litigation that the gravity of his injuries fulfils one of the foregoing tests, otherwise he is not to be entitled to continue the prosecution of his claim.
- (c) His right of recovery should be subject to the traditional rules of the law of negligence, so that the customary inhibitions of the fault system will apply.
- (d) The compensation which he may recover should be limited to non-economic losses for which no compensation is provided under the no-fault programme.
- (e) There should be a limit on the amount recoverable under this provision. The Committee considers that \$100,000 is a reasonable maximum.

In order to provide a source from which such compensation can be paid, it will be necessary to retain third-party liability coverage to the extent that such coverage is necessary to pay these "extra-ordinary" claims.

- 7. Own-vehicle coverage should also, in the Committee's opinion be, included in the overall no-fault programme to be adopted in Ontario. The Committee recognizes that there is by no means the same compelling importance about ensuring that *all* victims are compensated in own-vehicle damage cases as there is in bodily injury cases. Nevertheless, there are other reasons that are salient. At present, claims for vehicle damage outnumber bodily injury claims by eight to one. The result is that, when vehicle claim settlements are slow or inefficient or denied, a great many motorists who pay premiums year after year are likely to feel that they are not getting their money's worth out of the insurance system. Further-

more, the economies that can be achieved by eliminating fault investigations from bodily injury cases are even greater in vehicle damage cases, because of their greater frequency.

In addition, the accountability of the insurer to the insured is increased under a no-fault system. Under collision coverage, the insurer often pays his policyholder's claim with funds that he then recovers by subrogation from the insurer of the party at fault. That is, he is paying his policyholder with another person's money and consequently may not be concerned about controlling the appraisal process and the costs of repair. As a result, the incentive to contain costs under collision coverage is not as apparent as under no-fault coverage, where the insurer is, in all cases, accountable to his own policyholder for rising costs. **The Committee therefore supports** the principle of the inclusion of own-vehicle damage coverage within the proposed no-fault programme.

8. The method of inclusion of own-vehicle coverage within the proposed programme must make due allowance for two principal considerations. First, the purchase of own-vehicle coverage should be optional. Second, the Committee considers it essential,—particularly in view of Michigan experience and the Committee's observations in Massachusetts,—that there be a method of recovering deductibles to the extent that a driver is blameless, otherwise the programme will be unfair and thus unacceptable to the public. **The Committee therefore recommends** that:
 - (a) Every automobile policy should contain, as a *mandatory* feature, a new form of coverage under which the insurer will compensate the insured for his first \$250¹ of own-vehicle damage *to the extent that* the insured can establish his innocence in the accident, normally by means of a standardized collision assessment chart. However, no claim will be available against any third party, either by the insured or by his insurer through subrogation.
 - (b) Every insured should be able to purchase, if he so chooses, the usual own-vehicle coverage. If the insured has this coverage, his own insurer will compensate him for his own-vehicle damage above the amount of the deductible regardless of the insured's guilt or innocence in the accident. It bears re-iterating, however, that in no event will any claim be available against any third party, either by the insured or by his insurer through subrogation.
 - (c) Every insured should also, at his option, be able to purchase collision coverage in respect of limited recovery situations. If the insured has "limited own-vehicle damage coverage" his insurer will compen-

1. The Committee in its First Report recommended that the collision deductible be fixed at \$250, without the option of alternative amounts.

sate him for his loss over the deductible, but only to the extent that the insured can establish his innocence, normally according to the standards specified on a collision assessment chart or equivalent thereof. If the insured does not buy *any* collision coverage, his own insurer will not compensate him over the deductible amount, nor will he be entitled to seek recovery from any third party.

9. The Committee recognizes that the recommendations that it has formulated serve only as an outline for a new no-fault automobile insurance programme for Ontario. It also recognizes that there has not as yet been any opportunity to make any projections as to the cost of the proposed new system, although it is apparent that the savings to be gained from increased efficiency and the reduction in non-economic compensation claims will, in all likelihood, offset any overall increase in other claims costs. Exact dollar projections must inevitably be left to the industry and the Superintendent and a fine tuning of the terms can be conducted on the basis of that information.

DISSENTING OPINION OF:

Sam Cureatz, M.P.P.

Bud Gregory, M.P.P.

William Hodgson, M.P.P.

David Rotenberg, M.P.P.

Alf Stong, M.P.P.

Paul J. Yakabuski, M.P.P.

The Objective of a Motor Accident Insurance System

The principle that innocent victims should be compensated to the full extent of the damages they sustain lies at the very root of our value system and it is this fundamental principle on which our present motor accident insurance system is based.

It would be a mistake to reject this principle in favour of some principle that would purport to compensate all victims regardless of fault. Such a principle would compensate the drunken driver who has caused an accident with the same degree as it would compensate his victim. This would be done at the expense of awarding fair and ample compensation to the innocent. We reject a system based on this premise as unjust and unacceptable.

The automobile insurance system in Ontario has adopted in part the no-fault concept but it is essential to emphasize that it has done so without having to diminish the compensation payable to the innocent. The no-fault element that has been introduced is the Accident Benefits coverage that has been a part of our automobile insurance system in Ontario since 1972.

The present third-party coverage available to motorists in Ontario, to-

gether with its mandatory Accident Benefits coverage, now provides compensation for the vast majority of those who suffer loss as a result of motor accidents. Under the circumstances we believe there is no justification for drastic changes to the present system in order to provide some compensation for negligent drivers and those who at present choose either not to insure or to drive while impaired.

The Foundation of No-Fault

The concept of no-fault automobile accident compensation has developed in the United States in an atmosphere of deep dissatisfaction with the American system of claims settlement. These dissatisfactions were based primarily on four major weaknesses:

- (a) There was a grossly inordinate delay in the operation of the judicial process. As a result, cases often took a number of years to come to trial. Following trials, appeals could be instituted to effect still further delay.
- (b) Some American juries had a tendency to grant awards that were not only excessive, they were so excessive as to endanger the continued existence of the entire automobile insurance system. Damages for pain and suffering and other non-economic losses ran into the hundreds of thousands of dollars.
- (c) The American experience also included many instances of practices on the part of parvenue insurance companies that made a policy of delaying settlement as long as possible in the hope of discouraging claimants.
- (d) Many U.S. jurisdictions, having dropped their prohibitions of the contingency fee system of compensating lawyers in lawsuits, found that they were faced with an appalling escalation in legal expense. Fees amounting to thirty to forty percent of awards were not uncommon. When such legal expenses became generally known, juries often reacted by increasing their damage verdicts substantially with the view to enabling the victims to pay their legal expenses and still have enough left over to provide adequate compensation.

Because of these excesses, a school of thought has developed in the U.S. that considers that the abandonment of the fault system is justified in view of its demonstrable shortcomings and recommends the adoption of proposed no-fault systems in its place.

The situation in Ontario is entirely different from that which has been encountered in many American jurisdictions and it is important to list these differences:

- (a) In Ontario judicial delay has never been as serious as that which has been experienced in many American jurisdictions. When such delay has occurred, it has often been the result of delay on the part of claimants

who are anxious to demonstrate as fully as possible the full extent of their loss. At the present time progressive steps are being taken in Ontario to resolve such problems of delay as do exist and generally to expedite the conduct of actions through the Courts. Furthermore, the Ontario system of awarding costs in significant amounts has tended to act as a deterrent to unjustified appeals and this too has reduced delays in the judicial process. In short, the time lapse between the commencement of an action and its final adjudication is in general much shorter in the Ontario process.

- (b) Ontario courts have not experienced the American problem of unconscionable excessive damage verdicts. This is attributable in part to the different relationship that exists in Ontario between the judge and jury. Under our procedural system judges are much freer than their American counterparts to comment to the jury about the evidence and to make suggestions with regard to their verdicts. As a result Ontario juries have the benefit of judicial experience and advice to a degree that their counterparts in the United States have been unable to enjoy. The Ontario practice has also recognized the propriety of requiring non-jury trials where the evidence is likely to be unusually technical or complex and this too has resulted in greater stability in the amounts of awards. Whatever other favourable factors may have been at work in the Ontario judicial process, the fact is that the result has been a tradition of sane and realistic judgements.
- (c) While some degree of delay has often been involved in the negotiation of settlements between insurance companies and claimants in Ontario, there is little or no evidence to indicate that this process has been willfully protracted on the part of the industry for the purpose of discouraging claimants. It may be that this is attributable to the close and vigorous supervision that has been exercised by the Office of the Superintendent in Ontario. Far from seeking to effect delays, the industry in Ontario has demonstrated a constructive attitude by its efforts to expedite the settlement process. This has been done by the acceptance of the use of the collision charts and by the establishment of appraisal centres and by the industry-wide acceptance of the knock-for-knock principle in settling Accident Benefits claims.
- (d) Legal expense in Ontario has been more reasonable than in many American jurisdictions largely because of Ontario's prohibition of the contingency fee system. The result is that the general level of legal expense in motor accident claims in Ontario has never risen to the levels that have been reached in many American jurisdictions.
- (e) Investigations and observations that have been made in various jurisdictions have indicated that there is a significant variation from jurisdiction to jurisdiction in the litigiousness of the public. The popular willingness

to litigate in Ontario appears to be significantly below that of most American jurisdictions; claimants and industry representatives both appear to have a greater willingness to settle without resort to the courts. And the result is that the problems and expenses that litigation imposes upon a compensation system are much less in our jurisdiction than in many others. This of course is conducive to a prompter and more effective operation of the fault system.

In view of the differing conditions in Ontario, it would be a fundamental mistake to import into our law a solution that has been developed in other jurisdictions for problems that we do not have. The suggestion of insurance industry representatives speaking to the Committee during its deliberations in California would seem to be apposite: "If it's not broken, don't fix it!"

The Price to be Paid for a No-Fault System

The major price to be paid for a pure no-fault system is that it requires that innocent victims be deprived of their right to complete compensation so that those wholly or partly at fault can be compensated to the same degree as those who are innocent. While the Committee recommends a modified no-fault system to the extent that a victim of an accident may be entitled to recover compensation from a third party for non-economic losses such as pain and suffering, we reject the concession as inadequate in that the circumstances under which an innocent victim may claim are much too restrictive.

There is, however, a further price to be paid for no-fault as proposed by the Committee. The plan proposed by the Committee is premised on two faulty assumptions:

- (a) A change to no-fault will result in savings in administrative costs, these savings being attributable to the absence of a need to investigate fault; and
- (b) Reductions in loss payments attributable to the operation of the tort threshold provisions will offset the increased costs of the new no-fault benefits.

Neither assumption will prove out in the proposed plan.

First, while it is true that insurers will, in a significant number of cases, no longer need to engage in in-depth investigations or pursue judicial determination of the fault question, the Committee overlooks the fact that the proposed system will bring with it substantial new expense requirements which, in all likelihood, will outweigh whatever savings are obtained through elimination of tort suits.

Regarding the specific question of administrative expenses, the following new expenses will overcome the savings available through the elimination of tort cases:

- (a) Automobile insurers will be paying medical benefits on a first-party basis. These claims will require constant attention and control to avoid waste attributable to excessive or unnecessary medical care and treatment. This is obviously a considerable expense item made worse by the fact that the proposed medical benefits are unlimited in time. Accordingly, insurers may have to keep claim files open for the life of the victim and will have to maintain chronic control and surveillance of these files.
- (b) The same cost considerations apply to the proposed wage benefits. Again, it will be very expensive to maintain constant surveillance of these claims and to exercise control thereof so as to avoid excessive waste, fraud or duplication.
- (c) "Household replacement services" are unlimited in time, creating the same problems raised by the wage benefit.
- (d) Insurers will also have to open and maintain files for payment of first-party pain and suffering awards. Insurers currently have no experience with such payments anywhere on this continent and thus it is impossible to quantify this expense factor, although obviously it will be considerable.
- (e) Insurers will, for the first time, be paying survivors benefits unlimited in time, raising the same problems discussed under the wage benefit component.

On the basis of the foregoing, it is clear that the contemplated new system will reduce tort system expenses slightly (the very serious tort cases, which are the most expensive to administer, will remain in the tort system) but we believe that it will increase insurance company expenses so substantially that no significant administrative expense saving can be reasonably expected.

Let us turn now to review whether or not losses will be greater under the new system than those experienced under the current tort mechanism. Obviously some saving on the loss component will be realized through a reduction in the number of cases eligible for prosecution in court. But once more it must be emphasized that this saving cannot approximate that available in the United States since Ontario does not experience the expensive abuses which pervade the United States tort system. It is acknowledged that some loss dollars will be saved because of the tort threshold restriction. Further, some loss dollars will be saved through the proposed \$100,000 limitation on non-economic loss recovery, but since very few cases in Ontario currently exceed this \$100,000 loss figure, this provision serves more to reduce future costs rather than present costs. Thus, while some modest savings might be anticipated on the loss side, huge increases are inevitable under the proposed first-party benefit system.

Let us turn to examine briefly what comprises these new loss costs:

- (a) Insurers will be absorbing all costs currently incurred by the Ontario Hospital Insurance Plan attributable to the expense of providing medical care to "at-fault" automobile accident victims. Not only is this a new cost to the insurance system but it is a significant one, since as proposed insurers may be required to provide medical care and rehabilitation services to the victim for the balance of his life. These unlimited medical benefits are open to abuse and can be extremely expensive.
- (b) Wage loss, now with some restrictions, and household replacement services will be extended for an unlimited period of time, again requiring substantial cost increases.
- (c) The proposed schedule of first-party pain and suffering payments to be available to all, will create significant new costs which are impossible to identify because of the lack of insurance company experience with this novel kind of benefit scheme.
- (d) The extension of the survivors benefits to the dependants of "at-fault" drivers will represent a new and additional cost which can only be delivered to consumers at a very expensive price.

This in total, the proposed system will be a little less expensive to administer but the costs of providing the benefits thereunder will far exceed the benefits currently payable under the tort system. The net result is that the citizens of Ontario can likely anticipate significant price increases as a result of this proposed no-fault bodily-injury programme—a result directly opposite to their expectations.

No-Fault and Own-Vehicle Coverage

Approximately 75 percent of motorists in Ontario currently carry collision coverage providing for full compensation for their own-vehicle damage excepting only for the deductible portion thereof, which is usually \$100 or \$250.

The end result of the present situation is that there are only a very limited number of cases where own-vehicle damage cannot be recovered from one's own insurer and in these cases one is entitled to resort to the courts. This is in contrast to the situation that would exist under a no-fault system of own-vehicle damage compensation. Under the latter system, the claimant must have coverage to protect himself against another driver's carelessness, or he cannot recover his damages, even if he is blameless. In the case of the deductible, the best that a claimant can hope for is that he will be able to recover on the basis of a relatively rough-and-ready division of fault according to a collision assessment chart. If the chart does not entitle him to recovery, he has no resort whatever to the courts for redress. Experience in various other jurisdictions that have adopted the no-fault system,

notably the state of Michigan, indicates gross public dissatisfaction with the no-fault system because it precludes resort to the courts in such instances. This dissatisfaction reflects a fundamental public conviction that if one feels aggrieved one should have a right to sue in the courts.

In these circumstances it would appear self-evident that a no-fault system would not provide any advantage to Ontario's motorists that they do not enjoy under the present system.

Overcharging of Safe Drivers

A fundamental principle of insurance is that an insured person ought to pay premiums in relation to the risk that he imposes upon the insurance system. One major indicator of the actual extent of that risk is the insured's past record of having caused accidents by his negligence. In general, the no-fault system eliminates the best means of effectively forcing the high risk driver to pay the full share of the burden that he imposes upon the insurance system, by eliminating the statistical recording of at-fault accidents. Under a no-fault insurance system fault can only be reflected through the use of a driver offence surcharging system, and conviction surcharging has already proved to be unpopular amongst the public. As a result under the no-fault system, the excessive costs imposed upon the insurance system by the poor driver must be borne by the safer driver. The end result of this violation of a fundamental insurance principle is that the adoption of no-fault would result in the overcharging of the vast bulk of safe drivers.

Conclusions

The addition in 1972 of the Accident Benefits coverage to the Ontario automobile insurance system was intended to import into the existing system some part of the no-fault concept. At the same time it was intended to do so without detracting from the basic principle that the function of an automobile insurance system is to provide a means of paying full and fair compensation to those who suffer damage as a result of the conduct of those who are careless. Accident Benefits coverage will be enriched in the near future and it will be possible to do so, however, without jeopardizing the basic objective of the automobile insurance system.

Experience has shown that it is possible to proceed gradually and consistently with enrichment of the Accident Benefits coverage under controlled conditions so that the increases in costs do not go beyond affordability—and without jeopardizing the power of the system to provide adequate compensation to the innocent.

The objection to no-fault is not so much that it compensates the guilty as that it may compensate them at the expense of the innocent. Accordingly, the wise course to adopt in Ontario is to continue a policy of enrichment of Accident Benefits coverage so that even those who are at fault can be com-

pensated to some degree but only insofar as it is possible to do so without denying full compensation to the innocent and without rendering the insurance system excessively expensive.

For the reasons set out throughout the foregoing, the undersigned find that they must disagree with the majority of the Committee in its conclusions and recommendations in Part II of its Report and propose instead that:

- (a) The Province of Ontario reject any no-fault system of motor vehicle accident compensation, such as that recommended in Part II of this Report.
- (b) The Province of Ontario continue its policy of enriching the Accident Benefits coverage on a gradual basis, as experience shows that enrichment is affordable without jeopardizing the primary objective of granting adequate compensation to the innocent victim.
- (c) The automobile insurance industry in Ontario be given the opportunity to make further improvements and savings such as those that have already been effected as a result of the establishment of appraisal centres, the adoption of the collision assessment chart and acceptance of the knock-for-knock principle in Accident Benefits settlements.

PART III

GOVERNMENT PRESENCE IN THE AUTOMOBILE INSURANCE INDUSTRY

CHAPTER 9

The Experience with Government Ownership

A. INTRODUCTION

In this Part, the Committee proposes to consider the participation of government in the automobile insurance system, particularly with respect to the possible role of government as the owner of the insuring corporation, or alternatively as a rate regulator and supervisor of automobile insurance matters. Participation in the form of government ownership is discussed in Chapters 9 and 10, followed by a discussion of government regulation in Chapter 11.

In its First Report, the Committee stated:

“The Committee will seek to determine in detail the elements of public ownership of the automobile insurance business and how they vary from private ownership, with a view to making recommendations on this issue.”¹

Since beginning its investigation of automobile insurance, the Committee has had an extensive opportunity to consider the topic of government automobile insurance. Witnesses have been heard, the copious literature on the subject has been examined, and thorough reports have been received from the Committee’s consultants. In addition, the Committee held sittings in Regina, Saskatchewan and in Vancouver, British Columbia, where members had the opportunity of conferring with senior representatives of government insurance corporations and industry spokesmen. The results of all of these investigations are set out in detail in the Committee’s background study on “Government Ownership of Automobile Insurance” which begins on page 389 of this Report. This chapter contains a concise description of the Committee’s findings, followed in Chapter 10 by a statement of the conclusions that the Committee has reached.

B. GOVERNMENT OWNERSHIP IN OTHER JURISDICTIONS

Government ownership of the automobile insurance system is a perennial topic of political discussion, both in this jurisdiction and in a great many other areas of the world. For example, the Committee was interested to note during its recent deliberations in Boston, Washington, and Miami that although the operation of automobile insurance was solidly entrenched in the hands of the private sector in those jurisdictions, there, nevertheless, was some show of interest in government ownership, particularly on the part of consumer representatives and some government spokesmen. In view of this interest, it was tempting to presume that government owner-

1. The Select Committee on Company Law, *The Insurance Industry—First Report on Automobile Insurance*, Province of Ontario Legislative Assembly, 1977, page 242.

ship of automobile insurance was probably a widespread institution. The fact is that this is not so, and a survey of countries of the "western" world to determine which of them have adopted a governmental automobile insurance system helps to establish some perspective in the matter.

Of 88 jurisdictions that have recently been surveyed,¹ only 23 have adopted government automobile insurance. A breakdown of these jurisdictions by geographic area gives some further perspective on the matter. The following is a list of those jurisdictions:

In Africa:	Algeria, Benin, Peoples' Republic of the Congo, Ghana, Tanzania, Zaire and Zambia
In Asia:	Bangladesh, Burma, Indonesia, Korea, Sri Lanka and Peoples' Democratic Republic of Yemen
In Europe:	Czechoslovakia (no other communist block countries were included in the survey)
In Latin America:	Costa Rica
In Australasia:	Tasmania, Victoria, Western Australia and New Zealand
In North America:	British Columbia, Manitoba, Saskatchewan and Quebec (in part)

It is evident from this list that there are only a very few jurisdictions with government insurance that are in any way comparable to Ontario in terms of maturity of development or of basic political values. Indeed, apart from the three western Canadian Provinces, virtually all the other jurisdictions are too different, either in terms of economic circumstances or in terms of political outlook, to justify intensive study. In the case of Quebec, its entry into the field of government ownership is so recent that it has not as yet developed any body of experience to be examined.

Sweden has sometimes been perceived as being comparable in certain respects with the Province of Ontario and it was perhaps for that reason that the Committee at first presumed that some helpful lessons could be gleaned from that country's experience with government automobile insurance. Accordingly, when the Committee was conducting hearings in Zurich, Switzerland, it availed itself of the opportunity of conferring with Professor Jan Hellner of the University of Stockholm. The Committee discovered that, despite Sweden's widespread adoption of democratic socialism, it had not adopted government automobile insurance, and was unlikely to do so in the foreseeable future. The principal explanation apparently is that a large cooperative organization known as The Folksam

1. *Sigma*. The Publication of the Economics Department of the Swiss Reinsurance Company, Zurich, Switzerland, Edition 11/12, November/December 1977.

Group has secured a major place in the industry-operated automobile insurance system. The influence of this cooperative upon the insurance market has been such as to ensure that automobile insurance is provided to the consumer, by all companies, including the Group and insurers who compete with it, on such satisfactory terms that nationalization is simply not an issue. This is consistent with the Committee's more generalized observation, as a result of its investigations in a variety of jurisdictions: where the insurance industry is conducted in the interest of the consumer, there is little call for nationalization.

In brief, the three western Provinces appeared to offer by far the most fertile fields for the Committee's investigations.

C. HISTORY OF GOVERNMENT OWNERSHIP IN WESTERN CANADA

Saskatchewan established government auto insurance in 1946, when it established the Saskatchewan Government Insurance Office (S.G.I.O.) At that time only 12 percent of motorists were insured because coverage was virtually unavailable or unaffordable. Since then, S.G.I.O. has become solidly established as the exclusive carrier of basic automobile insurance within the Province. The terms of the coverage provided are substantially the same as those in effect in Ontario. However, the following forms of basic coverage are compulsory, and available only from S.G.I.O.: third-party liability coverage of at least \$35,000; Accident Benefits coverage; and collision coverage with a standard \$200 deductible in the case of passenger cars. "Extension coverage" increasing the limits or reducing the deductible is available from both S.G.I.O. and in theory from private companies. In practice very little automobile insurance is written by the private companies.

Manitoba concluded in 1970 that compulsory automobile insurance was desirable and in 1971 that a compulsory market should be served by a government automobile insurer. The Manitoba Public Insurance Corporation (M.P.I.C.) was therefore established as the exclusive carrier. As with Saskatchewan, the terms of the coverage provided are substantially similar to the terms in Ontario's standard automobile policy, but the following basic coverages are compulsory: third-party liability coverage with a minimum limit of \$50,000; Accident Benefits coverage; and collision-comprehensive coverage with a standard \$200 deductible on passenger cars. "Extension coverage" is available from both M.P.I.C. and private companies although, as in the case of Saskatchewan, little of this business is left for the private carriers to handle.

British Columbia created the Insurance Corporation of British Columbia (I.C.B.C.) in 1973, to be the exclusive carrier of compulsory automobile insurance throughout the Province. This decision appears to have been

motivated by a belief that a government corporation was the appropriate medium for marketing compulsory insurance, and by dissatisfaction with industry operations which included an unsolved residual market problem. Compulsory coverages consist of third-party liability coverage to a minimum of \$75,000, and Accident Benefits coverage. Collision and comprehensive coverage is optional, unlike the situation in Manitoba and Saskatchewan where it is compulsory. On the other hand, higher limits for third-party liability coverage and lower deductibles are available on an optional basis either from I.C.B.C. or from private industry. In practice at the present time the private sector sells only a trifling share of these optional coverages.

TABLE I
THE MOTORING AND INSURANCE ENVIRONMENT

Roads and Vehicles	Ontario	Manitoba	Saskatchewan	British Columbia
Drivers Licences (1975) (millions)	4.2	0.5	0.6	1.6
Total Motor-Vehicle Registrations (millions) (1975)	4.1	0.5	0.7	1.6
Passenger Vehicle Registrations (millions) (1975)	3.4	0.4	0.3	1.2
Miles of Paved Roads (1973)	38,200	6,800	11,300	16,500
Motor-Vehicles per Mile of Roads and Streets (1973)	37.3	9.2	4.2	33.4
Accidents (1975)				
Number of accidents	213,700	36,300	27,400	85,500
Number of Accidents per Hundred Vehicles	5.2	7.3	3.9	5.3
Accidents per Million Vehicle Miles:				
Property Damage	2.9	5.9	3.7	5.3
Injuries	2.5	2.3	2.4	2.3
Urban Accidents as Percent of Total	53%	79%	57%	70%
Traffic Laws				
Mandatory Seatbelts	Jan./76	No	Oct./76	Oct./77
Speed Laws	100 km/hr	100 km/hr	100 km/hr	100 km/hr
The Automobile Insurance Market				
Direct Premium Written, 1976 (\$million)	\$983.2	\$96.5	\$91.9	\$351.8
Size of Ontario Market Relative to other Provinces		10 times larger	11 times larger	2.3 times larger
Present Automobile Insurance Coverage				
Residual Market	6.7%	none	none	none
Accident Benefits Coverage	mandatory 1972	mandatory 1970	mandatory 1946	mandatory 1970
Uninsured Motorists				
At Present	7.12%	under 1%	under 1%	under 1%
Prior to Government Ownership	—	3% (1970)	88% (1946)	5% (1971)

Motorists with No Collision Coverage	25-27%	none	none	about 20-25%
Litigation				
Percent of Total Auto Claims			well under	
Resulting in Start of Court Action	2-3%	0.4%	1%	0.4%
Approximate Number of Lawsuits				
Filed, 1976	15,000	725	under 1,000	2,000
Lawsuits per 1,000 Registered Vehicles	3.6	1.4	1.4	1.2

Sources: Statistics Canada
S.G.I.O., M.P.I.C. and I.C.B.C.
Canada Safety Council
Insurance Bureau of Canada
Ministry of the Attorney General, Ontario
Report of the Federal Superintendent of Insurance, Business of 1976

The Motoring and Insurance Environment

It is important to have a clear perspective of the motoring and insurance environment of the western Provinces if one is to understand clearly their government automobile insurance systems. This environment is described in detail in Table 1.

The following features are particularly significant:

- Cars and Drivers:
 - Total numbers of cars and drivers are substantially lower than in Ontario.
- Roads:
 - The miles of paved roads are also very much fewer than in Ontario.
- Traffic Densities:
 - Much lower in Saskatchewan and Manitoba, but British Columbia is comparable to Ontario.
- Accident Frequencies:
 - British Columbia and Manitoba share high frequencies with Ontario, but Saskatchewan is less accident prone.
- Litigation Frequencies:
 - Lower in the western Provinces than in Ontario.

It bears repeating that the terms of the coverages available in these three western Provinces are fundamentally similar to those available in Ontario, in order to dispel any misconception that the government insurance Provinces provide forms of protection that are substantially different from those available in the other Provinces. There are, however, differences, as seen in Table 2. For example, in Ontario the minimum third-party liability limit is \$100,000, while such limits in British Columbia, Saskatchewan and Manitoba are \$75,000, \$35,000 and \$50,000 respectively. Accident Benefits coverage will soon provide for significantly higher payments in Ontario than in the other three Provinces.

TABLE 2
PRODUCT DESCRIPTION: ONTARIO AND GOVERNMENT AUTOMOBILE
INSURANCE IN MANITOBA, SASKATCHEWAN AND BRITISH COLUMBIA

	Ontario	Manitoba	Saskatchewan	British Columbia
A. Accident Benefits Compulsory Voluntary	Compulsory only under liability coverage	Yes No	Yes No	Yes No
B. Liability Coverage Compulsory Voluntary	No \$100,000 Minimum	\$50,000 Limit Extension	\$35,000 Limit Extension	\$75,000 Limit Extension
C. Collision Coverage Compulsory Voluntary	No With choice of deductible	Yes, \$200 deductible Lower deductible	Yes, \$200 deductible Lower deductible	No With choice of deductible
VENDOR	— Private Insurers	MPIC (public corporation) MPIC and private insurers	SGIO (public corporation) SGIO and private insurers	ICBC (public corporation) ICBC and private insurers
TYPES OF COVERAGES				

BASIC ACCIDENT BENEFITS		(Enrichments July 1, 1978)					
1. Death Benefits a) funeral expense b) death of household head c) death of spouse d) supplement for dependants e) limit	\$500	(\$ 1,000)	\$500	\$300	\$750		
	\$5,000	(\$10,000)	\$5,000	\$7,500	\$5,000 + \$75/104 wks.		
	\$2,500	(\$10,000)	\$2,000	\$3,000	\$2,500 + \$75/104 wks.		
	\$1,000 each no limit	(\$ 2,000)	\$1,000 each \$10,000	\$1,500 each \$15,000	\$1,000 + \$15/104 wks. each no limit		
2. Medical Expenses	\$5,000	(\$25,000)	\$2,000	\$4,000	lesser of \$100,000 or limit of liability		
3. Dismemberment (scheduled) Benefits	None		\$6,000 max.	\$10,000 max.	None		
4. Wage Loss Indemnity a) Total disability b) Waiting period c) Partial disability d) Injury to housewife	\$70/wk./104 weeks First day — \$35/wk./12 weeks	(\$140/wk.) (70/wk.)	\$75/wk./lifetime 7 days \$25/wk./104 weeks \$25/wk./12 weeks	\$60/wk./lifetime 7 days \$30/wk./104 weeks \$30/wk./12 weeks	\$75/wk./104 weeks 7 days — \$50/wk./26 weeks		
Premium Sources and Rating Criteria	1. Vehicle Premiums • age and sex • marital status • vehicle use • territory • value/size of vehicle	1. Vehicle Premium Fee • make, model, year, cylinders, body style of vehicle • vehicle use • territory 2. Driver Licence fee • age and sex and driver record 3. Gasoline Tax—2¢ per gallon	1. Vehicle Premium Fee • model, year and type of vehicle 2. Driver Licence Fee • \$5 plus surcharges based on demerit points 3. Gasoline Tax—3¢ per gallon	1. Vehicle Premium Fee • age and sex • marital status • vehicle use • territory • value/size of vehicle 2. Driver Licence Fee • charges based on demerit points			
	Risk Selection	No Risk Selection	No Risk Selection	No Risk Selection	No Risk Selection	No Risk Selection	No Risk Selection

The compulsory insurance rules in force in the three western Provinces apply to third-party liability coverage to the foregoing minimum limits and to Accident Benefits coverage. In addition, own-vehicle coverage with a standard \$200 deductibility is also compulsory in Manitoba and Saskatchewan, but not in British Columbia nor in Ontario. This Committee has recommended in its First Report that Ontario adopt compulsory third-party liability coverage, together with compulsory Accident Benefits coverage, with own-vehicle coverage to remain optional, and the government has indicated its intention of implementing this recommendation.

D. OPERATIONS OF THE GOVERNMENT CORPORATIONS IN WESTERN CANADA

Risk Selection

“Risk selection” is the process whereby insurance underwriters determine whether to accept an application for insurance, or whether to reject it because the risk that might be imposed upon the insurer is inconsistent with its insuring policies. The more discriminating the prevailing selection policies are, the greater the potential volume of uninsured drivers becomes.

Under the policies of the three government insurance corporations, all applications for insurance must be accepted with the result that there is no such thing as a “residual market” problem.

The Committee has already recommended in Chapter 3 that Ontario compel automobile insurers to “take-all-comers” for automobile insurance and that the industry be expected to establish its own pooling arrangements so as to share the risks imposed on the insurance system by unwanted policyholders.

Rating

Those responsible for rating, either in government insurance corporations or in the private sector, regularly face the need to balance social and actuarial considerations in determining the rates to be charged to various categories of vehicle owners and drivers. The view is generally held by the private sector that, as far as practical, insurance premiums should be based on actuarial considerations alone. This is intended to ensure that premiums charged to vehicle owners vary with the degree of risk of loss that they impose on the insurance system. It follows from this viewpoint that any cross-subsidization that is deemed “socially” necessary must be made outside the framework of the insurance industry by way of other forms of assistance. An example of such cross-subsidization in Ontario outside the insurance system is the flat \$10 vehicle permit fee charged to vehicle owners in Northern Ontario as compared to the significantly higher fees charged to owners in the rest of the Province.

A government insurance corporation is in an unique position in that it can balance social and actuarial considerations in establishing the insurance premiums to be charged to various categories of drivers. The one-company system makes it practical to fix rates so as to accomplish perceived social objectives, rather than on the basis of pure actuarial experience alone. All three western Provinces have taken advantage of this flexibility in varying degrees. On the other hand, the cross-subsidization that makes insurance more affordable to high risk drivers has become a source of some irritation to low risk drivers in British Columbia. As a result, revisions have been made and more are contemplated in the rating system so as to reflect greater actuarial realities. The experience of I.C.B.C. suggests that the government corporations' unique ability to cross-subsidize may not be an important advantage of government ownership.

It is impractical to carry out a cross-subsidization programme satisfactorily under a private sector insurance system. On the other hand, the need for such a programme may subside or even disappear under the no-fault system that the Committee has recommended in Chapter 8. One of the main consequences of a no-fault plan will be to reduce the importance of fault as an element in the ratemaking process. This will reduce the more extreme contrasts in premium rates between one driver and another.

Income Sources

Ratemakers for the government insurance corporations concentrate on a yearly determination of total revenue requirements by evaluating claims experience and expenses in accordance with substantially the same process that is followed by their counterparts in private company Provinces. However the sources from which those revenue requirements can be met are different. Depending upon the Province, monies may be available from gas taxes or drivers' licence fees as well as from the more traditional sources of direct premiums and investment income. The extent to which they rely upon these extraneous income sources is set out in Table 3.

TABLE 3
DISTRIBUTION OF INCOME COLLECTED BY
THE AUTOMOBILE INSURANCE FUNDS 1976

	Saskatchewan		Manitoba		British Columbia	
	\$Million	%	\$Million	%	\$Million	%
Certificate of Insurance Premium	\$57.5*	77%	\$72.3**	77%	\$347.3**	90%
Drivers' Licence Fees	*	—	10.6	11	7.5	2
Gasoline Tax	11.0	15	6.5	7	—	—
Investment Income	6.1	8	4.5	5	30.2	8
Total Revenues	<u>\$74.6</u>	<u>100%</u>	<u>\$93.9</u>	<u>100%</u>	<u>\$385.0</u>	<u>100%</u>

* Basic Coverage only, includes drivers' licence fees.

** Basic and Extension Coverage.

Source: Financial statements of S.G.I.O., M.P.I.C. and I.C.B.C.

It is only after allowing for these extraneous income sources that the balance of revenue requirements must be collected through premiums.

The consequence of the use of these extraneous income sources is firstly to impose some part of the cost of the insurance system upon drivers, rather than exclusively upon vehicle owners. Secondly, the use of the gas tax results in a further part of the cost of the insurance system being borne by motorists to the same extent that they use the roads and therefore to the proportionate extent that they are exposed to the risk of having an accident.

A further consequence, however, is that it becomes meaningless in many cases to compare premiums from jurisdiction to jurisdiction because, when taken alone, they do not always reflect the true costs of the automobile insurance system.

Use of Profits

All three government insurance corporations retain the profits from their operations and these are then used to absorb deficits, to reduce premiums in future years or to increase Accident Benefits.

Investment Policies

In the course of their operations, government insurance corporations generate large cash assets just as private companies do. These cash assets are invested to produce investment income in both instances.

Control of investment policy rests with each government insurance corporation and each follows a policy of concentrating its investments within its own Province to the fullest extent possible. S.G.I.O. and M.P.I.C. tend to invest in provincial, municipal and hospital bonds, while I.C.B.C.'s current policy is to invest in local short-term securities. These investment assets do not constitute a significant portion of the totality of local provincial investments.

Marketing

The government insurance corporations have minimized their marketing costs in different ways.

First, the government corporations issue an insurance certificate rather than a full copy of the policy, and the result is some saving in paper work.

Second, sales of automobile insurance are tied to the issue and renewal of licence plates, and sales are connected in varying degrees with the operations of the local Motor Vehicle Licencing office. In Manitoba and British Columbia particularly, the local insurance agent is also the local licence agent, although in Saskatchewan only about one-quarter of the insurance agents are also licence agents. To the extent that savings are achieved, they are reflected in reduced marketing costs.

Third, the role of the agent is changed. He relies almost exclusively upon the government corporation for the automobile segment of his business. On the other hand, the agent no longer incurs heavy mailing charges for policy renewals or changes; he no longer has accounts receivable or bad debts; and the entire transaction process is simplified. In addition, in many instances, the agent is able to add licence renewal commissions to his insurance revenues. At the same time, the agent's remuneration has been substantially reduced. Commissions amount to about 4 percent, 3½ to 4½ percent and 8 percent of premiums earned in Manitoba, Saskatchewan and British Columbia respectively. In Ontario, commissions average about 14 percent of premiums earned.

Enforcing Compulsory Insurance

Experience in many jurisdictions leads to the conclusion that the most effective system of enforcing compulsory insurance is to establish a plate-to-owner system together with an irrevocable policy system, tied to the issue or renewal of licence plates. The three western Provinces have virtually succeeded in achieving this system. In each Province a plate-to-owner system has been established. In each case, an insurance renewal is a prerequisite of the plate renewal. In Saskatchewan, all premiums are payable in cash. Manitoba and British Columbia allow the premium to be paid by instalments, however in the case of delinquency payment is normally recovered by seizure of plates, or by refusal to issue plate renewals until the unpaid instalments are paid up. The insured may not cancel his policy without surrendering his plates. The result is a nearly perfect system of ensuring that virtually all drivers are insured at all times.

Claims Handling and Settlement

The operation of a provincial automobile insurance system through a single government corporation simplifies claims handling. One insurer deals with all claims involved in an accident insofar as compulsory coverage is concerned and, since the government corporations also carry the bulk of optional coverage, insofar as the bulk of the "extension" coverage claims are concerned as well. As a result, claims are normally settled without any inter-company disputes, thereby providing a saving. Indeed where both parties to an accident carry collision coverage, as is notably the case in Saskatchewan and Manitoba where collision coverage is included in the compulsory package, there can be no dispute about the insurer's liability except possibly with respect to the deductibility element.

The government insurance corporations have established Claims Centres where the entire adjusting process can be conducted under one roof: repair costs are appraised, policy records are examined, and claimants' entitlements can be settled in a one stop operation. Outside the three Provinces, private insurers have established appraisal centres but to date these

have not evolved into fully coordinated, one stop centres for the entire settlement of claims.

As a part of the same processes described above, the resort to litigation has been minimized by the one-company system. As the data in Table 1 indicate, litigation volumes are very substantially lower. It should be added by way of qualification that it has not been possible to determine whether relatively generous settlement policies may have contributed to these low levels. It does appear, however, that on occasion the public has taken advantage of the governmental purse, as when I.C.B.C. was in its start-up stages.

Administration

Government automobile insurance corporations can take advantage of their size in achieving economies of scale. For example, highly advanced computerization is in effect in British Columbia and Manitoba, while Saskatchewan is currently planning improvements. In addition, these corporations have the benefit of on-line retrieval of Motor Vehicle Bureau driver accident and offence records.

Economies of scale extend into the field of repair costs where training programmes are conducted for adjusters and appraisers, and research can be conducted into repair techniques. These are facilities that might be difficult to maintain under a multi-company system in the western Provinces because of the relatively small size of the local business units involved. On the other hand, the dominance of the government corporation in the automobile insurance market has on occasion resulted in serious disputes with the repair industry. In such a situation, the governmental nature of the corporation can conflict with its responsibility to minimize policyholders' claims costs.

S.G.I.O. operates its own integrated salvaging business and retails parts out of its own warehouses. The result is a saving in repair costs. Whether such vertical integration should be construed as an exercise in insurance cost saving or as a dubious expansion process is a matter for debate.

The government insurance corporations tend to resort to reinsurance through the international markets much as the private companies do. However, with recent escalations in premiums, the government corporations have begun to reduce their reinsurance programmes wherever it is practical to do so. There is no evidence that the outflow of private sector funds into reinsurance premiums was a problem that contributed to the decisions to establish the government insurance corporations.

E. FINANCIAL COMPARISONS

Comparing Premiums

Information received by the Committee implies that premiums charged in the western Provinces are generally lower than Ontario premiums. How-

ever, there are very real dangers in seeking to draw any inferences from these apparent variations. Differences in geography and vehicle population explain most of the variance. Driver categories used for setting premium rates are different. The method of allocating loss costs amongst various driver categories is different in that the Ontario process tends to be based largely on actuarial considerations while in these western Provinces the process includes some consideration of extraneous factors, such as the financial capacity of the under 25 driver. Furthermore, there are differences in claim costs per accident from one Province to another. Finally, insurance revenues derived from "gas" tax in Saskatchewan and Manitoba and from drivers' licence fees in all three Provinces also tend to make it meaningless to compare the individual premiums in the various jurisdictions.

Comparing Operating Costs

A second basis of financial comparison is concerned with the operating costs of the government insurance systems and the private industry system in Ontario. This comparison involves a complicated process which is explained in full detail in Background Study Two to this Report. The comments and qualifications contained in Section E of that study are very important to an accurate understanding of the comparisons.

Many factors complicated the Committee's analysis of the comparative operating costs. The practices followed by the government insurers and their operating results during the period examined by the Committee rendered accurate comparisons with each government corporation and then with the Ontario industry to be difficult. Differences in accounting methods, sources of revenue and the fact that the government corporations are not subject to corporate income taxes contributed to the complexity of the comparison.

Access by government insurance corporations to possible hidden subsidies or services which were not accounted for in their annual published reports was another matter of difficulty for the Committee. In this regard, the Committee's consultants have made extensive and repeated investigations. As a result of their findings, the Committee is inclined to the conclusion that there are no significant hidden subsidies or "free rides" that would materially distort the financial information under consideration.

Recognizing the above difficulties the Committee, however, considered it useful to quantify, in very rough terms, the apparent spread of operating costs between a government insurance system and the private industry system in Ontario. This was accomplished in the following manner:

- (1) The operating results of the three government insurance corporations, as published in their annual reports and certified by the auditors, were analyzed in considerable detail. Five years experience, 1972-1976, was included for M.P.I.C. and S.G.I.O. and three years 1974-1976 for I.C.B.C.

- (2) Because S.G.I.O. results on extension coverage for the period under review were not available, the S.G.I.O. ratios utilized were for basic compulsory coverage only. This exclusion does not have a material effect on the resultant ratios.
- (3) Average operating ratios were developed for each government insurer which eliminated certain extraordinary one time costs and operating losses and adjusted the corporations' operating results to a break even level.
- (4) These average ratios were then utilized to develop a representative operating cost structure for a government insurance corporation which is presented in Table 4.

TABLE 4
GOVERNMENT INSURANCE CORPORATIONS
ESTIMATED OPERATING COST STRUCTURE

	M.P.I.C.	S.G.I.O.	I.C.B.C.	A Government Insurer
	%	%	%	%
Operating Costs				
Acquisition (including Premium Taxes)	6.3	6.5	7.1**	6.6
Underwriting and Policy Processing	1.7	3.6*	6.3	3.8
Claims Adjusting	7.9	7.4	6.2	7.2
General Administration	2.1	4.3*	2.5	3.0
Total Operating Costs	18.0	21.8	22.1	20.6
Investment Income	(4.2)	(8.5)	(5.8)	(6.2)
Net Operating Costs	13.8	13.3	16.3	14.4
Claims Incurred	86.2	86	83.7	85.6
Premiums Earned including Extraneous Sources of Income	100.0	100.0	100.0	100.0

* Allocated on same ratio as M.P.I.C.

** No premium taxes in British Columbia.

By the further allocation of general administration expenses, the estimated cost ratios of the three major financial components of a government insurance corporation may be derived. These are outlined in Table 5 and are compared to similar costs which the Committee has estimated for the private industry system in Ontario. Details of these estimates for the Ontario industry are presented in Chapter 12 of this Report.

TABLE 5
APPARENT SPREAD OF OPERATING COSTS BETWEEN
A GOVERNMENT INSURANCE SYSTEM AND
PRIVATE INDUSTRY IN ONTARIO

	Government System	Private System	Apparent Spread
Acquisition	8%	18%	10%
Underwriting and Policy Processing	5	8	3
Claims Adjusting	8	15	7
Total Estimated Operating Costs as Percent of Premiums Earned	21%	41%	20%

The Committee observes that it is extremely difficult to determine, with any degree of accuracy, the precise amount of the spread of operating costs between a government insurance system and private industry. However, in order to permit a better perspective on the structural differences between the private industry system in Ontario and a government insurance system, as described elsewhere in this Chapter, some quantification of the cost differences was in order. The total spread of 20% is consistent with the amount described by representatives of the government insurers as realistic.

Comparing "Pass-through" Efficiency

The third and most practical basis of financial comparison is the ratio of claims payments to total automobile insurance expenditures. This measure is most appropriate because of the intrinsic nature of automobile insurance systems: essentially they are systems whereby money passes into them, and the bulk of it passes through and is used to pay claims. Their financial efficiency can be judged by the percentage of insurance expenditures that they must retain to pay the expense of the "passing through" operation.

Table 6 is designed to show claims payments as a percentage of total expenditures. It has been prepared again from information published in the annual reports of the government insurers for the periods indicated. When considering the table, the following observation is also significant: the relatively higher ratios of the government insurance corporations would be misleading if their claims payments were excessively high, say, because of excessive generosity in adjusting practices. However, the Committee has found no significant evidence of this, except in the organizational stages of I.C.B.C. The extent of this exception is not quantifiable.

TABLE 6
COMPARISON OF CLAIMS INCURRED TO TOTAL EXPENDITURES
(Based Upon Average Statistics)

	Ontario Industry* (1971-1975) (\$ million)	M.P.I.C. (1972-1976) (\$ million)	S.G.I.O. (1972-1976) (\$ million)	I.C.B.C. (1974-1976) (\$ million)
Total Expenditures	594.8	59.8	50.9	296.5
Claims Incurred	378.3	49.5	42.1	224.9
% of Total Expenditures Returned as Claims	63.6%	82.8%	82.7%**	75.9%

* The Select Committee on Company Law, *First Report on Automobile Insurance*, page 190

** Results of basic compulsory coverage only, when adjusted to reflect extended coverage experience, produce an efficiency measurement in the range of 80%.

Source: Background Study Two to this Report.

The conclusion to be drawn from the foregoing is that in the periods under review, 63.6 percent of the Ontario industry's expenditures went to pay claims, whereas in the case of M.P.I.C., S.G.I.O. and I.C.B.C. respectively, about 82.8 percent, 80 percent and 75.9 percent of expenditures went to pay claims. In short, these western operations were about 12 to 19 percent more efficient than the Ontario industry in terms of this method of comparison.

The average statistics shown in Table 6 have not been adjusted for extraordinary expenses such as the amortization of start-up costs or the large initial losses in the case of I.C.B.C. Accordingly, it is evident that the government insurance corporations have been unable to achieve the maximum amount of the spread of 20% identified in the previous section. M.P.I.C. and S.G.I.O., the smaller and established government insurers, have operated at a level which comes close to this spread. It remains to be seen whether the I.C.B.C. operation, with its much larger size and greater relevance to Ontario, will be able to do so consistently.

Observations on the Apparent Spread in Operating Costs

In the Committee's judgement, "efficiency" or the apparent spread in operating costs between the private industry system in Ontario and the government insurance systems is a composite of the following factors:

1. Because of its monopolistic nature, the government insurer need not incur those costs expended by a private insurance company to ensure the maintenance or expansion of its competitive market position.
2. As a result of economies of scale and major structural differences between the government and private industry systems, the government insurer experiences a lower level of administration and delivery costs.

Offsetting the above factors in some part might be a potential for inefficiencies in some aspects of the government insurer's operations because of the lack of competition.

The Committee wishes to make it abundantly clear that considerable care should be exercised in the interpretation of the above observations. Differences in the product and the product mix and the possibility that the government organizations may have some access to free services or cost sharing not available to private companies renders a definitive conclusion difficult. Also, the "low-cost" certificate of insurance premium paid by consumers in the government ownership Provinces is somewhat of an illusion as it is only one of a number of sources of income used by the government insurance corporation to support the automobile insurance system. Differences in corporate income tax status encountered under the two systems and also the differences in personal income tax rates in the various Provinces add yet another dimension to the evaluation of the ultimate relative positions of the consumer.

In further explanation of its extensive deliberations on the matter, the Committee observed that the amount of the spread in operating costs attributable to the monolithic nature of the government insurer could not be objectively determined and, accordingly, this amount was not pursued.

The lower level of administration and delivery costs which is experienced by the government insurance system, however, was a matter which was considered by the Committee with considerable interest. Those elements of government ownership which might be capable of emulation by private industry were investigated in greater detail and the Committee's conclusions and recommendations on these matters are presented in Chapter 13 of this Report.

CHAPTER 10

Conclusions on Government Ownership As an Alternative for Ontario

The members of the Committee are agreed upon the facts about government insurance corporations that are set out above. They have not, however, reached agreement upon the interpretation that should be placed upon those facts nor upon the recommendations to be made upon the question of government insurance. The interpretations and recommendations that are set out below are therefore followed by the dissenting opinion of Messrs. Germa, Renwick and Warner.

The following are the Committee's interpretations and recommendations with regard to government ownership of automobile insurance.

1. *An examination of government automobile insurance jurisdictions throughout the world indicates that government ownership, far from being an "idea whose time has come" is an idea that has been adopted in only a relatively few western jurisdictions.* Most of the jurisdictions that have adopted a system of government automobile insurance tend to be either less developed economically or less stable politically than Ontario. While this does not of itself dictate that proposals for government insurance should be rejected, it does suggest that they should be approached with caution.
2. *One of the arguments advanced for the establishment of government insurance systems in Western Canada, was that if all members of the motoring public are compelled to buy insurance, they should not thereby be compelled to contribute to private sector profits.* The Committee does not agree that this contention is a justification for the adoption of a government insurance system. Under the economic system of this country, with its own characteristic mix of private sector and governmental activity, and indeed under many more socialized economic systems, it is generally accepted that the private sector should supply a broad variety of goods and services that are essential in their nature. By and large the private sector performs this role competently and in a way that justifies the making of profits. If the private insurance companies fulfil their role under a compulsory insurance regime in Ontario, they too should be entitled to make a profit. The Committee therefore rejects this contention. It should be added that, while the enactment of the compulsory insurance rule certainly does not dictate that automobile insurance should be "nationalized", it does necessitate that automobile insurance should be supervised carefully in the public interest. This matter is dealt with in the following chapter.
3. *There is a popular misconception that the government automobile insurance corporations in Western Canada provide terms of coverage for*

the consumer that are unlike those provided in the private sector Provinces. It is quite clear that this is untrue. The terms of the traditional coverages, third-party liability coverage, Accident Benefits coverage and own-vehicle coverage, are substantially the same as those available in Ontario. Indeed, Ontario's minimum liability limit and its recently enriched Accident Benefits are more generous than the protection provided in the western Provinces.

It is true that the government insurance Provinces have given lengthy consideration to the adoption of broader no-fault systems, and Quebec has actually established such a system insofar as bodily injury compensation is concerned. On the other hand, there is no indication that either system is inherently better suited than the other to the operation of a no-fault automobile insurance programme such as the one which is proposed in Chapter 8 of this Report.

4. *Under a government automobile insurance system, all applications for insurance must be accepted, with the result that there is no "residual market" problem.*

The Committee has concluded that one of the gravest shortcomings of the private insurance system is the perennial problem of the residual market. For the moment the problem appears to be relatively less serious, because the industry currently has ample capacity, but it was only recently that the problem was critical and, unless a real and permanent solution is found, risk selection policies will again become more discriminating, "creaming" will again become more rigorous and the problem will again reach critical proportions. This is a long standing pattern in the industry.

The Committee recognizes that, under a government insurance system, the residual market ceases to be a problem, and the Committee considers this as a major benefit to be derived from such a system. This is especially important when compulsory insurance legislation comes into force because, if a government licenced driver must have insurance in order to drive, government must surely see to it that insurance is available.

Instead of recommending government auto insurance as a solution to the problem of the residual market, the Committee repeats its recommendations that two alternative steps be taken. First, licenced automobile insurers should be compelled to take all comers. Second, the industry must be responsible for the establishment of a method of pooling of its own devising so as to spread the cost of servicing the residual market equitably amongst all insurers and across the entire automobile insurance system. This must be done in such a way that those transferred into the residual market are fairly treated. The Committee expects that the industry will fulfil this responsibility.

5. *A one-corporation system is able to provide one common classification system for the entire Province.* This is in contrast to the present system in Ontario, whereby different insurers are able to use different classification systems. However, the Committee is satisfied that its recommendations contained in Chapter 15 will provide Ontario with a mandatory standard classification system that will help the consumer to shop intelligently for insurance.
6. *The one-corporation system makes it practical to fix rates so as to accomplish perceived social objectives, rather than on the basis of pure actuarial experience.* In contrast the private sector holds to the view that premiums should be fixed purely on the basis of actuarial considerations and that any cross-subsidization that is deemed "socially" necessary must be made outside the framework of the insurance system.

Under the one-corporation system, if there is a perceived need for social values to influence premiums, for instance if there is a consensus that some subsidization should be provided to the under 25 driver, such cross-subsidization must be balanced by the principle that an insured ought to pay for the risk that he imposes on the insurance system, and no more. In Saskatchewan, dissatisfaction with the cross-subsidization of urban drivers by rural drivers is sometimes expressed. In Manitoba there has been public criticism because of a belief that rates for older drivers are fixed such that young drivers are subsidized and that "all-purpose" and pleasure drivers' premiums are unfairly paying the burden imposed on the system by business drivers. Finally, in British Columbia, I.C.B.C. originally established a rating system that subsidized younger drivers and residents of certain rating territories at the expense of the rest of the driving community and the result has been a public protest. These experiences suggest that a government corporation's unique ability to cross-subsidize can be more of a liability than an asset.

It is impractical to carry out a cross-subsidization programme satisfactorily under a private sector insurance system. On the other hand, the need for such a programme may subside or even disappear under the no-fault system that the Committee has recommended in Chapter 8. One of the important consequences of this plan will be to reduce the importance of fault as an element in the ratemaking process. This will reduce the more extreme contrasts in premium rates between one driver and another, such as the contrast involving the under 25 driver, and it will accomplish this in a manner that is entirely consistent with sound actuarial principles.

7. *A government insurance system can draw upon extraneous revenues such as drivers' licence fees and gas taxes, so that it is not limited in its*

revenues to premiums and investment income. In this respect the government corporation has some advantage over the private company system. There is no practical way of distributing such revenues amongst private insurers, even if it were desirable to do so.

Two advantages flow from this characteristic of the government corporation. First, through the medium of drivers' licence fees, the cost of the insurance system can be spread so that drivers as well as owners bear some part of that cost. Secondly, by means of a gas tax, there can be some direct relationship between the number of miles that a motorist drives and therefore the extent of his exposure to the risk of accident, and the amount of his contribution to the insurance system. The Committee recognizes these advantages but it has concluded that they are not of a compelling nature.

The Committee also considers that the use of such extraneous revenues may disguise the real cost of an insurance system. In contrast, the private sector system has the advantage of making consumers more aware of the cost of the automobile insurance system.

The Committee also recognizes a very real disadvantage in this characteristic of government insurance corporations. Because of the ever-existent possibility of revenue manipulation, there is always a possibility that revenues or expenses will be manipulated for political purposes that are not relevant or are inimical to the sound operation of an automobile insurance system.

8. *One stop Claims Centres can be established by government insurance corporations with the result that there is a significant increase in convenience to the motoring public.* Such centres are well-suited to government insurance operations, where there can be no disputation between insurance companies as to the fixing of fault or the cost of repairs. This advantage diminishes as private insurance companies evolve co-operative methods of claims settlement such as the I.B.C.-sponsored Appraisal Centres and the use of collision assessment charts to settle disputes. As indicated in Chapter 13, however, the Committee is convinced that further improvements can be made by the Ontario industry.

The establishment of a no-fault auto insurance system, as recommended by the Committee in Chapter 8 of this Report, would provide the opportunity to move even further to cooperative methods of claims settlement. A no-fault system by removing disputes over fault simplifies the adjusting process to a settlement procedure concerned with quantum only. As a result, companies might be more willing to adopt a system wherein independent or industry-hired adjusters perform the adjusting function in an all industry Claims Centre.

9. *Government insurance corporations invest their premiums received in advance and reserve funds in accordance with governmentally established investment goals.* The Committee may have some concern about the excessive caution with which private companies invest but there has been almost no suggestion that insurance companies have failed to invest fairly in this Province. Indeed, in Ontario, most private company investments are in government securities that are hardly different from the securities in which the government corporations invest. The Committee does not see any distinctive characteristic in government ownership insofar as the investment policies of the government corporations are concerned.
10. *The adoption of government automobile insurance facilitates the establishment of a fully effective system of enforcing compulsory insurance by providing for the close integration of the vehicle licencing and automobile insurance systems.* As a result, the concept of an irrevocable policy coterminous with a valid licence plate has been successfully implemented.

The Committee considers that this is a major feature of the government insurance system, and it considers fully effective enforcement to be fundamental. However the Committee is still convinced that the private sector, despite some protestations, will be able to develop through joint efforts with government an efficient compliance system as envisaged in Part I of this Report, including an irrevocable policy if necessary. Until such time as the industry seems unable to do so, the Committee sees no compelling advantage to this particular characteristic of government insurance.

11. *One-corporation insurance systems are said to be especially well-suited to the operation of worthwhile ancillary activities such as safety research, loss prevention programmes, auto repair studies and driver education programmes.* While this appears to be true, the Committee has observed that the private sector has been very effective in carrying out jointly sponsored projects, particularly through the auspices of the industry-wide Insurance Bureau of Canada. Such joint ventures also include extensive statistics gathering programmes and the establishment of appraisal centres. The Committee has concluded that the demonstrated ability of the companies to work together on such projects leaves little significant advantage to the government corporations.
12. *The level of apparent efficiency of the government insurance corporations is higher than that of the Ontario insurance companies.* The Committee has taken great care in reviewing the basis for this comparison. It repeatedly asked its consultants to reinvestigate the information that they had obtained. It weighed carefully the qualifications which were made on the comparison. It has concluded that, while the financial in-

formation may not be exact in every detail, it is substantially correct and the comparisons which have been made are fair in substance. However, the Committee cannot fully quantify the higher efficiency of the government insurance system.

Having reached that conclusion, the Committee, nevertheless, considers that the apparent relative inefficiency of the industry in Ontario is of serious concern. It is strongly inclined to believe that improvements may be achieved in the operating cost structure of this industry, certain of which may find their origin in the operating methods of the government insurance system.

13. The Committee has concluded that any higher efficiency afforded by the monopolistic nature of a government insurance system does not, by itself, justify a change to government insurance for Ontario. This is because the difference in efficiency is not the only test by which insurance systems should be judged. In addition to consideration of dollar efficiency there are other factors to be weighed; for instance, there is a weight or value to be given to such advantages of the competitive system as the ability to choose between companies.
14. *Part of the difference in efficiency mentioned in conclusion 12 can be traced to the fact that the selling costs of private insurers in Ontario are higher than in the three government insurance Provinces.* This difference between the two systems appears to constitute the largest single cost difference between them. It has been suggested to the Committee that a justification for at least part of this difference is the provision of more individual service to the public under the private system. Whether or not this is true, the Committee is convinced that the industry should nevertheless be able to take major steps to streamline its marketing process so that these expenses can be reduced. Part IV of this Report reviews this matter in detail.
15. *A further explanation for the difference in efficiency described in conclusion 12 is that claims costs for adjusting and settlement are higher in Ontario.* The government corporations enjoy the advantage of one stop claim centres, and it is clear that this advantage is a major cause of the difference.

In Ontario there are counter-balancing factors. There has been a steady improvement over recent years in the degree of cooperation that the Insurance Bureau of Canada (I.B.C.) has succeeded in promoting amongst automobile insurers. This new spirit appears in the establishment of a chain of Appraisal Centres, in the use of collision assessment charts and other cooperative techniques for settling claims. It is reasonable to hope that this evolutionary process will continue and the Committee would expect to see some closing of this gap in the margin of

efficiency. This matter is more fully considered in Part IV of this Report.

The implementation of the Committee's recommended no-fault programme will also reduce adjusting costs substantially. Most of the cost of investigating and litigating liability claims should be saved. The great bulk of claims will involve only the insurers and their own insureds. Consequently, insurance companies should be able to settle claims with the same efficiency that now exists under the "one-corporation" systems in the West.

16. *Underwriting and policy processing costs are apparently higher in Ontario.* Although this difference in degree of efficiency is one of the less substantial savings features, the Committee would hope that the industry would succeed in reducing this gap in the coming years.

It is true that a large government insurance corporation such as I.C.B.C. should be able to take advantage of certain economies of scale that are not available to smaller insurance companies. And yet Ontario's larger automobile insurers, even though smaller than I.C.B.C., should be large enough to enjoy similar economies. Ontario companies should also be able to increase their use of various cost saving joint projects under the aegis of the I.B.C. Whatever methods are adopted, it is clear that the private sector must increase its efficiency in order to survive in a world in which not only insurers compete against each other, but also entire insurance systems compete for favour.

17. *The Committee has given due consideration to some of the consequences that might reasonably be expected to flow from the adoption of a government automobile insurance system for Ontario.* Automobile insurance constitutes a significant portion of the entire field of general insurance in Ontario. There is a real danger that, if the industry were forced out of the automobile insurance field, there would be an adverse impact on the entire general insurance field.

Many companies that have enthusiastically conducted integrated general insurance operations in the Province might well suffer a loss of ardor if automobile insurance were excluded from their portfolio. This is particularly likely in view of the very substantial part that automobile insurance plays in the overall field of general insurance. The result might well be a significant withdrawal from the general insurance field, with resulting problems of lack of capacity in such other crucial areas as property insurance.

It is not possible to forecast the full extent of these consequences.

18. *The monopolistic nature of the government corporations, which is said to be the source of much of their strength is also, in the Committee's opinion, the source of their potential weakness.* Recently established

monopolies may operate efficiently for differing periods of time, depending upon the persistence of their founders' and managers' enthusiasm. In the two western Provinces that the Committee visited, it was quite apparent that those who had created and who were managing the government insurance corporations had continued to be entirely devoted to the efficiency of their operations.

However, the Committee remains concerned that when there is no competitive atmosphere to force operating efficiencies upon management, the eventual result might be inefficiency. It has been argued that under our system of government the pressures that elected representatives bring to bear upon government enterprises are an adequate substitute for the competitive forces of the market place. In an era when government activities have become so widespread, this simply cannot be true.

However, to point to this danger in a government monopoly is not to reject the government insurance corporation for all time and under any circumstances. Rather it is to emphasize that, whatever the present weaknesses of the private sector may be, and whatever the contrasting appearance of strength of the government monopoly, the government monopoly carries within itself a weakness that must inevitably be weighed in the balance.

In summary the Committee has concluded, after weighing the various characteristics of the government automobile insurance systems, that Ontario can be better served under a system of automobile insurance operated within the private sector than by the adoption of a government automobile insurance system.

The Committee has not reached this conclusion, however, without certain reservations, the principal of which are:

- (a) that it is imperative that the industry resolve the chronic problem of the residual market;
- (b) that a generally acceptable and well-publicized classification system must be developed and that public confidence be established in the ratemaking process;
- (c) that the industry cooperate in the development of a fully effective compliance system as part of the implementation of compulsory insurance in the Province;
- (d) that any future increases in selling expenses be curtailed through careful programmes designed to make marketing systems more efficient;
- (e) that any future increases in adjusting expenses be curtailed by continued inter-company cooperation and by the implementation of the Committee's cost saving no-fault programme; and

(f) that any future increases in administration expenses be contained.

The Committee recommends that the Superintendent of Insurance should follow a policy of giving continuous encouragement to the development of programmes within the industry in Ontario for the purpose of achieving the foregoing goals,—goals that the Committee believes that the industry can achieve. Then after a five year period an appropriate Legislative committee should re-assess the progress that has been made and should review the conclusions that have been reached in this Report.

DISSENTING OPINION OF:

Bud Germa, M.P.P.

James A. Renwick, Q.C., M.P.P.

David Warner, M.P.P.

It is with regret that we dissent from the major conclusion reached by the Committee “that Ontario can be better served under a system of automobile insurance operated within the private sector than by the adoption of a government auto insurance system”. Indeed, the conclusion of the Committee, when read with the major reservations about the private insurance industry, can only be considered as a counsel of delay and not as a definitive conclusion about the merits of a government system. It is a counsel of delay because the Committee proposed that, after a five-year period of stringent monitoring of the private insurance industry through the Office of the Superintendent of Insurance, another committee of the Assembly should reassess the industry and review the conclusion reached in this Report.

It is, in our opinion, much too long a time before the people of Ontario will have the benefit of a government auto insurance system.

The work of the Committee and the results of that work set out in the First Report and in this, the Second Report, underscores dramatically that there are major problems in the auto insurance industry. Merely to correct those problems and to implement new solutions where required will, even if wholeheartedly undertaken by government, take a long time. It is our view that these major changes in the industry must be undertaken urgently but should only be undertaken along with a definite and fundamental commitment by the government to introduce a government auto insurance system. If such a commitment were made now, the people of Ontario would have the benefit of a first class government system within five years without waiting for further study and possible implementation some time after 1985.

The First Report of the Committee stated that the Second Report of the Committee would deal with the question of the government presence in the auto insurance industry and, in particular, with a government-operated system. It has therefore been possible for the first time in Ontario for a committee of this Assembly to look objectively and carefully at the experience of

the three auto insurance systems in force in Manitoba, Saskatchewan and British Columbia. Until this time, the whole question of government-operated auto insurance has been bedevilled by ideological confrontation. The Committee has now had the opportunity to examine the significant benefits in cost and efficiency which the citizens of Ontario would realize if a system modelled on those of the three western Provinces were now implemented.

It is not without significance that the systems in those Provinces, although established by New Democratic Party governments, were not changed in any significant respect, let alone abolished upon the return to power of a Social Credit Party in British Columbia, a Liberal Party in Saskatchewan and a Conservative Party in Manitoba. If the so-called disadvantages of such government systems of auto insurance were real, then no doubt at least one, if not all, of those Parties with political philosophies of free enterprise, differing significantly from the philosophy of the New Democratic Party, would have attempted to abolish these government-operated systems. That this has not happened is a most significant and telling fact in favour of these systems.

The Committee has had the benefit not only of meetings in Saskatchewan and British Columbia, but also had the benefit of in-depth research, analysis and comparison prepared for the Committee by its consultants and reflected in Background Study Two—Government Ownership of Automobile Insurance—included as part of this Second Report.

It would be our expectation that this Second Report, particularly in those areas dealing with private versus public ownership of automobile insurance, will now be studied objectively throughout the Province in anticipation that the people of the Province will recognize the significant advantages in cost and efficiency of a government system.

Based on the background study referred to above, the Second Report sets out eighteen matters that anyone considering the introduction of a government auto insurance system must assess, weigh and balance. Having done so, it is our opinion that objectively no one can escape the conclusion that, overall from a consumer viewpoint, a government auto insurance system would be more efficient than the private industry system because a government system in Ontario would return a higher percentage of the total premium dollar to the consumer or conversely, could result in a reduction in automobile insurance premiums. In the three western Provinces, and after all direct subsidies such as drivers' licence fees and gas tax revenues were considered, there was no evidence that this higher return to the consumer resulted from any distortions of the systems, nor were the insurance policies and coverages provided by those government systems substantially different from that now available in Ontario.

We have further taken into account, expressing this opinion, that under a government system corporate taxes on auto insurance business, such as income tax, would not be paid.

It is with considerations of cost savings to the consumer with no loss of efficiency and service in mind, that we respectfully dissent from the Committee's conclusion.

CHAPTER 11

A Government Presence in Rate Regulation

A. INTRODUCTION

In the preceding chapter, the Committee recorded its conclusion that the business of automobile insurance should continue to be conducted in Ontario by the private sector, but that there was nevertheless a supervisory function which should be exercised by government, particularly when automobile insurance becomes compulsory. Governmental supervision of the automobile insurance industry can most conveniently be considered in three broad areas: regulation of the rates charged by insurers, solvency regulation, and regulation of all other aspects of the business, particularly marketing and adjusting. This chapter deals with matters of rate regulation and is supplemented by Background Study Three on "A Government Presence in Rate Regulation" which begins on page 477 of this Report. The other supervisory functions of the Office of the Superintendent of Insurance are summarized in Appendices I and J. However, any more intensive consideration of the responsibilities and operations of the Superintendent's Office is deferred to a later stage in the Committee's deliberations, so that the Committee will have obtained a proper perspective for considering the presence of the Superintendent in *all* of the various fields of insurance.

Every North American jurisdiction currently exercises some form of rate regulation with the exception of Illinois, Prince Edward Island and Ontario. This chapter summarizes the history of rate regulation in various jurisdictions and discusses the question of need for regulatory legislation in Ontario, including the relevance of recent federal competition policy proposals. Some further comments about the meaning of "open competition" then lead to an exploration of alternative rate regulatory systems for Ontario and a discussion of their relationship to solvency regulation.

B. HISTORY

In Canada

Although *federal legislation* has provided for an Office of the Federal Superintendent of Insurance since the nineteenth century, his chief function has always been to ensure that all federally incorporated and licenced companies under his supervision are able to meet their policyholders' valid claims. While this function indirectly involves a review of premium rates to the extent of ensuring that they are not so low as to jeopardize the solvency of the insurer, rate regulation normally connotes a monitoring of rates with the emphasis on seeing that they are not excessive, inadequate or unfairly discriminatory. These latter criteria have not been a part of the Federal Superintendent's area of concern.

Provincial legislation has provided for a Provincial Superintendent of Insurance in each Province to supervise provincially incorporated or licenced companies. The primary concerns of these Superintendents have always been matters of licencing, solvency, and the fairness of insurance contracts to the public. However, the problem of rate regulation has also been of concern to the Provincial Superintendents, this being an issue that gained attention as early as the 1920's and 1930's.

In 1930, as a result of popular dissatisfaction with rates in effect at that time, *Ontario* established a Royal Commission on Automobile Insurance Premium Rates under the Honourable Mr. Justice Hodgins. In his report he recommended the enactment of compulsory insurance legislation and added as a corollary, that when a compulsory law is passed requiring people to procure a policy of insurance, there ought to be government regulation of the price. He accordingly recommended that legislation be enacted empowering the Ontario Superintendent to order, after due notice and a hearing, an adjustment of automobile insurance rates whenever they are found to be "excessive, inadequate or unfairly discriminatory or otherwise unreasonable".

The Province's response was the inclusion of sections 365 to 367 in The Insurance Act, but these sections have never been proclaimed in force.

In 1968, *British Columbia* created a Royal Commission on Automobile Insurance. It recommended that a three-man Automobile Insurance Board should be established with power to fix a maximum rate for the compulsory coverage policy, to monitor insurance rates in the Province and generally to act as an investigative and appellate tribunal over complaints about automobile insurance. The Board actually came into existence for a brief time, but it became redundant upon the creation of the Insurance Corporation of British Columbia.

Nova Scotia in its turn appointed a Royal Commission on Automobile Insurance in 1973. This commission concluded that the administration of automobile insurance ought to be left in the hands of the private sector but that additional government control should be exercised through the Office of the Superintendent and that this control should include the regulation of rates by the Superintendent. These recommendations have not been implemented, so that rate regulation remains in the hands of the Nova Scotia Board of Commissioners of Public Utilities as it was prior to the Royal Commission's Report.

Ontario commissioned a further study during the period from 1973 to 1975 and on this occasion Douglas H. Carruthers, Q.C. (now the Honourable Mr. Justice Carruthers) reported. He recommended a broad range of reforms which included reference to rate control. Essentially, he proposed a system that would encourage price competition in that it would allow consumers to see clearly the price and nature of the product that was offered so

that there could be ready comparison. He did not recommend any more stringent system of rate regulation.

The present state of rate regulation in the Provinces can be summarized as follows:

- British Columbia, Saskatchewan and Manitoba: Basic automobile insurance is sold by government insurance corporations and no regulation of their rates is considered necessary. Optional "extension coverage" may be sold by the private sector but the extent of their market share has not warranted the giving of any consideration to the need for any rate regulation. The most effective control over private company rates is the rate structure at which such coverage is available from the government corporations.
- Quebec has recently limited private sector participation to property damage coverage and has required the filing of rate manuals within ten days of the promulgation of any rate change. Any future action that the government plans has not yet been made clear. There is no suggestion that there is to be any supervisory authority over the rates of the new government insurance corporation.
- New Brunswick, Nova Scotia, Newfoundland and Alberta now have their own rate regulatory tribunals. In the first three, rate regulation is exercised by the Public Utilities Commissions; whereas in Alberta, it is exercised by a more specialized Automobile Insurance Board. All of these tribunals function under rate regulatory systems that require approval or deemed approval of rate changes prior to their being put into effect.
- Prince Edward Island and Ontario have no working legislation providing for rate regulation in the customary connotation of that term.

Ontario's present situation is briefly as follows: the Superintendent exercises a broad active role in supervising the licencing of companies, in monitoring their marketing and claims settling conduct including their relationships with individual consumers, and also in providing a vigorous regulation that is designed,—and very successfully designed,—to prevent insolvencies. In this area of solvency monitoring the Superintendent clearly has power to act if rates are so low as to endanger a company's solvency.

The solvency aspect of regulation, however, is designed to ensure that legitimate claims, when presented, will be paid. Rate regulation, on the other hand, implies broader forms of consumer protection with controls over inadequate rates being only one of the factors which are controlled or supervised. With rate regulation, regulators must also ensure that rates are not excessive or unfairly discriminatory. Rate regulation, therefore, is meant to include "helping people get the most insurance for their money . . . in simple words . . . the public purpose of insurance regulation".¹

1. State of New York, *The Public Interest Now in Property and Liability Insurance Regulation*—A Report to Nelson A. Rockefeller by the State of New York Insurance Department, 1969, page 12.

Sections 365 to 367 of Ontario's Insurance Act would provide, if proclaimed, for the prohibition of unfair discrimination and for the Superintendent to order adjustments in rates which he may find to be excessive, inadequate, unfairly discriminatory or otherwise unreasonable.

These sections have heretofore been perceived as some sort of Damoclean sword hanging over the industry's head, ready to have their effect if occasion should warrant. However in 1976, a substantial disagreement arose between industry spokesmen and representatives of the Superintendent's Office as to the justification of proposals for substantial rate increases. The Committee had the opportunity of observing and deliberating upon this debate and it was not clear whether the threat of proclamation of the "Hodgins' sections" had any influence on the decisions of the industry. It would appear that in fact these sections, so long as they remain unproclaimed, have little or no effect.

In the U.S.A.

As a result of complex constitutional measures, the business of insurance is subject to state regulation although it is constitutionally possible for the federal government, if led by Congress, to assert an overriding authority in this area. In order to preserve their powers, the states have had to enact some form of regulation of the insurance business. Insofar as rates are concerned, this has generally taken the form of rules that rates should not be "excessive, inadequate, or unfairly discriminatory".

While the various states have enacted a variety of legislative policies relating to rates, these can conveniently be classified into two main groups: "rigid rate regulation" laws and "open competition" laws.

Rigid rate regulation laws are of three broad forms:

- Statutory bureau laws or state-made rate laws are regulatory systems under which the authority assumes the initiative for fixing rates. Insurers must then charge the fixed rates, no more and no less.
- Prior approval laws are regulatory systems under which insurers are prohibited from changing their rates upward or downward without first obtaining the approval of the authority.
- Sometimes there is a variation to provide that the insurer may file its application for approval and may then put its change into effect until ordered to stop. Alternatively, the rule is varied so that the insurer may file and implement its new rates if the authority issues no notice of objection within a short time after filing.

The essence of these systems is that rates are fixed or approved by governmental authority and changes are permissible only with the sanction of that authority. The industry feels that these systems of rigid rate regulation have discouraged rate reductions, contributed to instability in the industry, im-

posed unnecessary restrictions on collective merchandising and direct trading and have aggravated the availability problem.

The term "open competition laws" refers to a system whereby direct regulation of specific rates is replaced with a system under which regulation is directed to ensuring that fully competitive conditions exist in the market place, upon the theory that competition will then spontaneously minimize premium rates. In 1947, California enacted an open competition law and still follows that system. It has concluded that the system produces a rate structure that is responsive to costs, that encourages innovation in the form of coverage and rating classification plans, and that encourages entry into the business in the state. The State Insurance Department polices the industry through periodic rating and underwriting examinations conducted by its rate regulatory division. In addition, there are solvency reviews that are conducted by a separate field examination division.

The Committee has visited California and has conferred at length with its regulatory officials who reported their conviction that their form of rate regulation was the most effective mechanism for providing a reliable and efficient insurance system. They recommended certain tests to measure the extent to which competition existed in any insurance market place including:

- The degree in which the market was concentrated in individual companies or groups;
- The extent of price variations between competitors;
- The ease of entry to or exit from the market place;
- The availability of economies of size in the industry;
- The growth pattern of the market; and
- The solvency of insurers.

Recent trends in American rate regulation philosophy lead away from direct rate regulation and toward open competition systems with their emphasis on independent pricing instead of fixed rates. One-third of the states have already made the change and this trend has earned the support of the National Association of Insurance Commissioners.

In 1977, the U.S. Department of Justice completed a sophisticated study on the *Pricing and Marketing of Insurance* and concluded among other things firstly, that rigid rate regulation had had adverse effects on the availability of coverage at reasonable cost and secondly, that vigorous competition is a more desirable substitute for rigid rate regulation.

Clearly, the immediate future of rate regulation in the United States is directed away from fixed rate systems and toward open competition. The Committee is intrigued with this approach, particularly as a result of what members learned from their discussions with regulators in California. The Committee has hypothesized that Ontario, having had no system of rate reg-

ulation for many years, may now be well advised to leapfrog over the more rigid methods of regulation that American jurisdictions have found wanting to adopt the more flexible and more sophisticated open competition concept. In brief, regulation in Ontario should combine the best of this Province's experience with the best of experience that can be gleaned elsewhere.

C. OBSERVATIONS ON THE ONTARIO SYSTEM

Representatives of the industry in Ontario maintain that the Ontario market place is now competitive in nature and that it accordingly ensures the best possible deal for the consumer. They hope that, if there is to be any additional regulation, it will not interfere more than minimally with their operations. Representatives of the Superintendent's Office confirm the existence of a competitive atmosphere in the Ontario insurance industry and also agree that the normal market forces provide an effective control over automobile insurance rates.

The Committee nevertheless has some concerns or comments that can be expressed as follows:

- a) Legislation regarding rate regulation has passed the Legislature but it has never been proclaimed in force. As a result, the function of the Superintendent in the area of rate regulation has been limited to the publicizing of increases that have been judged by the Office to be unfair.
- b) As a result of the foregoing, the Superintendent's activities have focused on solvency regulation, that is to say, upon ensuring that companies remain solvent. In this area, the Superintendent's Office has done a creditable job, as witnessed by the almost total absence of insolvency in the industry.
- c) While competition may indeed exist in the Ontario market place, the traditional emphasis on solvency has overshadowed any intensive and conclusive study of the existence or extent of such competition.
- d) The Committee feels that Ontario's traditional emphasis on solvency should continue so that when claims are presented, they will be certain to be paid. In addition, in the Committee's opinion, more emphasis is required in Ontario on rate regulation in order to achieve a better balance between financial stability and the other objectives of rate regulation.
- e) If there is to be a reliance upon competition to provide continuously greater benefits to the consumer, it would seem appropriate that a mechanism should be established so as to ensure that the monitoring and encouragement of competition is carried out on some regular periodic basis.
- f) Any proposal for the formalizing of the "open competition" philosophy into the Ontario system of insurance industry regulation is complicated

by the problem of division of legislative powers by the Canadian constitution. At present, the federal Combines Investigation Act occupies the field of competition regulation. The only area left open to the Province is that of rate regulation which would require the approval or disapproval of specific rates, an approach that is the opposite of the open competition approach. However, the present Combines Investigation Act is likely to be replaced with a new federal Competition Act, the terms of which are not known with any certainty.

g) In the Committee's opinion, governmental encouragement of competition must always be considered in the overall context of all forms of insurance industry regulation. In other words, the related topics of solvency and competition regulation should be reviewed simultaneously by considering the following matters:

- The formulation of detailed criteria as to what constitutes open competition in the market place and what constitutes anti-competitive business conduct.
- The methods to be adopted to enforce compliance with rules that prohibit anti-competitive conduct.
- The appropriateness of existing "in-house" solvency and liquidity rules in protecting the public interest.
- The advisability of providing legislative sanction for any new rules for monitoring competition, and more specific legislative sanction for in-house solvency and liquidity rules.

The Committee has had the opportunity to review various aspects of the above matters in the context of automobile insurance and comments on its conclusions in a later section. In the succeeding sections two ancillary questions are examined: first, what criteria can be used to determine the effectiveness of competition; and, second, the role of the Superintendent's Office and the appropriateness of "in-house" rules in the context of any new regulatory requirements for protecting the public interest.

D. WHAT IS EFFECTIVE COMPETITION?

The purpose of encouraging open competition in the automobile insurance industry is to ensure the existence of a *reliable* insurance mechanism that:

- Makes coverage universally available,
- Maximizes the service that is provided,
- Minimizes the price in relation to cost, and
- Encourages innovation.

With this purpose in mind, it is possible to glean from experience and observation in various jurisdictions some criteria for determining whether open competition exists in the market place. The following tests have been

developed primarily from the Report of the British Columbia Royal Commission on Automobile Insurance of 1968 and from the Insurance Bureau of Canada's 1974 study, "Competition, Economic Efficiency and Profitability in the Canadian Property and Casualty Industry", as referred to in Background Study Three to this Report. While these tests are by no means exhaustive, they give a reasonable indication of the characteristics that must be encouraged if open competition is to provide its greatest benefits.

a) Structure of the Industry

- There should be a sufficiently large number of firms to provide customers with alternative sources of supply.
- No firm or groups of firms acting in concert should be able to exercise monopoly power.
- The more firms, the better.
- No firm should have an exceptionally high level of market concentration unless other factors exist which provide a counter balance, such as ease of access to the market place.
- The easy ability of other firms to gain access to the market place is of itself a substantial criterion.
- The existence of incentives for firms to make competitive innovations such as price cuts, product innovations or improvements to the production or marketing processes.

b) Conduct of the Industry

- Firms should behave independently, with each seeking to improve its own profits. For example, there must be no agreement on prices.
- Actions should not be taken for the purpose of excluding actual or potential competitors from the market place, or for the purpose of restricting their ability to compete.
- No firm should be a price leader whose pricing practices are followed by the others in the industry.
- Similarly, a governmental authority should not fix a price that is to be generally followed, if open competition is to exist.
- Improved products and economic progress result in a market place in which competitors search for a temporary monopoly through product differentiation.

c) Market Performance

- If the response to increased demand is increased prices and not increased output, there is an indication that effective competition has ceased.
- The introduction of cost reducing innovations leading to the reduction of prices and the growth of the market is indicative of the existence of open competition.
- When prices are inflexible so that they are totally unresponsive to

changes in the forces of supply and demand, there is an indication of lack of competition. Conversely, price responsiveness is indicative of the existence of open competition.

- The existence of unfair price discrimination; that is to say, where the same price is charged for two disparate forms of the product (as where two identical policies, each bearing a different degree of risk, are sold at the same premium), there is evidence of monopoly power if the practice is followed on a continuous and regularized basis.

It is one thing to formulate criteria to determine the existence of open competition and it is quite another matter to determine how they are to be applied to a specific industry or firm. The conclusion drawn by the Committee from these studies is that the development of such criteria and the way they are to be applied in the course of governmental supervisory operations are matters of great complexity and sophistication. Accordingly, the foregoing criteria are considered by the Committee to be examples only. Further study is required to formulate a complete set of criteria that can be incorporated into a fully detailed system of rate regulation based on the principle of open competition.

E. OTHER ASPECTS OF REGULATION

In considering new requirements for a greater government regulatory presence in automobile insurance, the Committee believes that attention should also be devoted to the present in-house tests and rules applied by the Superintendent's Office and their appropriateness in protecting the overall interests of the public. Accordingly the Committee has reviewed the present "solvency and liquidity" rules and the intent or purpose which is served by their application. These rules are outlined in some detail in Appendix I to this Report. Furthermore the Committee examined the present responsibilities and operations of the Superintendent's Office in order to determine, among other things, what functions the Office might be able to assume should changes be made in regulatory requirements. A general review of this matter is provided in Appendix J to this Report.

These studies provided a valuable context to the Committee in considering the matter of rate regulation in this Province. However, the Committee believes that it is not appropriate to address final recommendations on these matters until its review of the other-than-life components of the industry is completed. In particular the Committee notes that both the present in-house solvency and liquidity rules and perhaps some of the alternatives for increasing the government's regulatory role over rates may apply to all insurers incorporated in Ontario, not only automobile insurers.

Accordingly, the appropriateness of these rules and regulatory requirements cannot be considered properly until the Committee has completed its review of the other-than-life components of the industry and considered the

need to expand government supervision to include these components. Only then will the Committee be able to evaluate the ramifications of its recommendations on the Superintendent's Office. Accordingly, the Committee must also defer its final review of the responsibilities and functions of this Office until all questions regarding the insurance industry are raised.

Included in the Committee's further study will be two further aspects which the Committee feels should be addressed in the context of the entire industry:

- a) reinsurance and the part it plays in insurance costs; and
- b) appropriate requirements for foreign and branch office reports to the Superintendent.

F. CONCLUSIONS AND RECOMMENDATIONS

The Committee has reached the following conclusions:

1. In recording its conclusion in the preceding chapter that the business of automobile insurance should continue to be conducted in Ontario by the private sector, **the Committee also concluded** that there is a fundamental need, particularly when a compulsory automobile insurance rule is established, for a governmental presence in the field of automobile insurance supervision and this applies specifically to rate regulation.
2. **In the Committee's opinion**, more emphasis is required in Ontario on rate regulation in order to achieve a better balance between financial stability and the other objectives of rate regulation.
3. There are three major methods of rate regulation. The first involves a rigid rate regulation system under which a governmental authority fixes maximum rates, exact rates or a range of rates and these govern the charges that may be made for the various categories of risk. An insurer is then prohibited from violating these rigid standards.

Secondly, rate regulation can also take the form of a prior approval system wherein insurers must apply for approval of all rate changes before the rates can be put into effect.

The Committee rejects these types of regulation as a long-term, or permanent approach to rate regulation. The Committee has observed that such systems do not encourage rate reductions, nor do they even ensure that rates are kept to a minimum which is consistent with financial stability, affordability, and universal availability of coverage.

The third major method of rate regulation involves the use of a body of regulations designed to perpetuate fully competitive conditions in the market place. This is termed "open competition rate regulation". This method is based upon the theory that such competition will in itself minimize premiums and ensure the existence of a reliable and efficient insurance system.

4. **The Committee has concluded** that open competition rate regulation is the form of automobile insurance regulation which is best suited to the present market conditions in the Province of Ontario.

While there would appear to be competition in the Ontario automobile insurance market place at the present time, the Committee has, however, observed that there are no formal set of criteria for recognizing competitive conditions and for monitoring business activity in such a way as to promote a maximum of competition. Accordingly, the Committee has concluded that there is a need to carry out studies that will formulate a complete set of criteria for evaluating competition, and will permit the establishment in the immediate future of a fully detailed system of rate regulation based on promoting open competition.

5. An open competition system of rate regulation must not be considered out of the context of the overall topic of regulation and supervision of insurance companies; especially in relation to solvency and liquidity matters. **The Committee therefore proposes** to proceed, as it reviews other forms of general insurance, with a more detailed investigation of the entire topic in the course of its consideration of the role and function of the Superintendent's Office. This detailed investigation will include:

(a) An Open Competition System

- The development of a suitable set of criteria for evaluating competition.
- The establishment of the methods and mechanisms, including public reporting requirements, needed for regularly monitoring the existence and extent of competition in the Ontario insurance industry.
- The advisability of legislating these new requirements or providing for them in regulation.

(b) Solvency and Liquidity

- Further consideration of the appropriateness of the solvency and liquidity rules as they pertain to the other-than-life insurance industry.
- Further consideration of the need to supplement or amend the present solvency and liquidity rules to make them more meaningful to present conditions.
- The advisability of legislating these rules or new requirements or providing for them in regulation.

The Committee will instruct its staff to work closely with the Superintendent of Insurance on these matters. Recommendations will then be submitted in the context of the entire other-than-life insurance industry, rather than within the constraints of this Report on automobile insurance. In order to provide broader safeguards to the public interest in Ontario,

the Committee is hopeful that this investigation will achieve the appropriate balance between the surveillance of insurance company solvency and the other objectives of rate regulation.

6. While the Committee rejects rigid rate regulation as a long-term, or permanent approach, it nevertheless recognizes that some readily-available stop-gap method of controlling rates may become necessary in the short-term, pending the formulation of the more sophisticated long-term solution. **The Committee therefore recommends** that consideration be given to the review and proclamation of sections 365 to 367 of The Insurance Act and the granting to the Superintendent of more effective powers for enforcing compliance with those sections if the need should appear necessary in the interim.

PART IV

**MARKETING, ADMINISTRATION
AND CLAIMS ADJUSTING COSTS**

CHAPTER 12

The Operating Cost Components of The Ontario Automobile Insurance Industry

A. INTRODUCTION

Premiums paid by Ontario automobile insurance policyholders will exceed \$1,000,000,000 in 1978. Improvements to the present system resulting in the achievement of only a small percentage reduction in costs to premiums earned could save Ontario consumers several millions of dollars. These savings could be used to reduce premiums or alternatively to enrich the benefits presently paid to claimants. Because of the vast size of the automobile insurance industry, significant savings can result from a very small adjustment in the operating cost structure.

Accordingly, in its First Report, the Committee commented as follows:

“Many questions have been raised by the Committee concerning further details about marketing, administration, and claims adjusting costs as they apply to various types of coverage, various rating categories, various deductible limits, and the various elements of claims adjusting costs.

The Committee will identify in detail major cost elements and will develop overall analyses of the costs of marketing, administration and adjusting claims”.¹

In this chapter, the Committee outlines the major operating costs experienced by the Ontario automobile insurance industry and, in the following chapter, examines areas with potential for savings through improvements to the present system in this Province.

B. OPERATING COSTS UNDER THE PRESENT ONTARIO SYSTEM

The various operating functions of the automobile insurance system in Ontario can be grouped into three major components: marketing or acquisition, underwriting and policy processing, and claims adjusting. The administration function forms a part of each of the three major components.

In preparing its First Report, the Committee was acquainted with the difficulty in accumulating the financial results and operating costs of the industry in Ontario but was able to provide the industry “average” results for the period 1971 to 1975, as outlined in Table 1.

1. Select Committee on Company Law, *The Insurance Industry—First Report on Automobile Insurance*, Province of Ontario Legislative Assembly, 1977, page 242.

TABLE 1
AUTOMOBILE INSURANCE INDUSTRY-ONTARIO
ESTIMATED INCOME STATEMENTS FOR THE YEARS
ENDED DECEMBER 31, 1971 TO 1975
(in millions)

	Total 1971-1975	Annual Average 1971-1975	Annual Average Percentage
Premiums earned	\$2,753.3	\$550.7	100.0%
Claims incurred	\$2,125.0	\$425.0	77.2%
Commission expense	386.7	77.3	14.0
Premium tax	57.3	11.5	2.1
General expense	405.1	81.0	14.7
Investment and other income	(260.2)	(52.0)	(9.4)
	<u>\$2,713.9</u>	<u>\$542.8</u>	<u>98.6%</u>
Profit before income taxes	<u>\$ 39.4</u>	<u>\$ 7.9</u>	<u>1.4%</u>

Source: Select Committee on Company Law, *First Report on Automobile Insurance*, page 190.

Representatives of the Insurance Bureau of Canada have reviewed these statistics and have agreed, in general terms, that the percentages are representative of the on-going operation cost structure of the industry. These statistics, however, do not provide sufficient cost detail on the major functional components of the automobile insurance system.

In 1969, the Insurance Bureau of Canada implemented an "Expense Allocation and Reporting System" which is currently utilized by the majority of its members. By utilizing the data reported by member companies in 1974 and 1975, it has been possible for the Committee and its consultants to gain further insight into automobile insurer operating costs and their functional components. In so doing, it is recognized that some aspects of the functional components of expenses will differ among insurers, particularly in the case of direct writers.

It has been possible to capture considerable additional information on expenses from this analysis. However, details on the most significant component of cost, namely claims incurred and other direct costs of adjusting and settlement, are not collected by the Expense Allocation and Reporting System, such that it has been necessary to retain the assumption, taken from the industry "average" results, that claims expenses charged directly to claims incurred would be in the range of 11-12% of premiums earned. Representatives of I.B.C. feel this assumption was reasonable during the 1971-1975 period under review but point out that the use of appraisal centres and other recent efficiencies will cause this estimate to be too high in the future.

The functional cost components of the Ontario automobile insurance system are outlined in Table 2, based on a restatement of the 1971-1975 industry "average" results. Identified direct administrative costs are then allocated to the major functional components of the system. Appendix K

TABLE 2
ESTIMATED OPERATING RESULTS
ONTARIO AUTOMOBILE INSURANCE INDUSTRY

	1971-1975 Annual Average Percentage	Allocation by Functional Operating Cost Components				Total
		Allocation by Detailed Components (Appendix K)	Acquisition	Underwriting/ Policy Processing	Claims Adjusting	
Premiums Earned	100.0%	100.0%				
Claims Incurred	77.2	66.2				
—Direct Cost of Claims Incurred		11.0			11.0%	
—Adjusting Costs		14.0	14.0%			
Commission Expense	14.0	2.1	2.1			
Premium Tax						
General Expense	14.7	1.5	1.5			
—Agent Service and Promotion		5.5		5.5%		
—Underwriting/Policy Processing		2.6			2.6	
—Claims Adjusting Administration		5.1	1.0	2.5	1.5	
—General Administration		41.7	18.6	8.0	15.1	41.7%
Investment and Other Income	(9.4)	(9.4)				(9.4)
Profit Before Income Taxes	1.4%	1.4%				32.3%
Total Operating Costs:						

outlines the assumptions and the detailed analyses of the 1974 and 1975 I.B.C. data used to reallocate direct and general administrative costs on a functional component basis. As a result of this allocation process, the *total* costs of the present automobile insurance system in Ontario can be expressed on the basis of its major functional components as shown in Table 3. For the most part, the estimated breakdown of costs compares with the data produced by the I.B.C. Expense Allocation and Reporting System. Claims expenses charged directly to claims files and investment income are not collected by the I.B.C. system.

TABLE 3
COSTS OF ONTARIO SYSTEM BY
FUNCTIONAL COMPONENTS 1975

	Percent of Premiums Earned	
	Estimate for the Industry	I.B.C. Reporting Members
Acquisition	18.6%	17.9%
Underwriting and Policy Processing	8.0	7.6
Claims Adjusting		
—Administration	4.0	3.6
—Direct Costs	11.0	126.3% of premiums written)
	15.1	
Total Costs	41.7	
Investment Income	(9.4)	
TOTAL OPERATING COSTS (per Table 2)	32.3%	

* Converted from Direct Premiums Written in the same proportion of Total Premiums Earned to Total Premiums Written

This analysis has permitted the Committee to identify in an approximate manner the major elements of costs in the Ontario automobile insurance system. In the next chapter, the Committee considers possible opportunities for improvement in each of the functional cost components.

CHAPTER 13

Opportunities for Operating Cost Savings in The Ontario Automobile Insurance Industry

In this chapter, the Committee examines the opportunity for savings in the functional cost components of the present Ontario automobile insurance system and provides conclusions regarding the need for improvements.

In the following discussion, the Committee makes reference to certain of the procedures and concepts inherent in the government ownership systems in Manitoba, Saskatchewan and British Columbia. The Committee believes it is worthwhile to examine these systems in order to determine whether certain features, if adopted by the private sector in Ontario, might improve efficiency. In this regard, the Committee makes reference to the government insurers' marketing, administration and claims adjusting procedures described in Background Study Two to this Report on "Government Ownership of Automobile Insurance".

A. ACQUISITION AND AGENCY SERVICE

As outlined in Chapter 12, the total estimated costs of the marketing or acquisition function in the Ontario industry system are as follows:

	Percent of Premiums Earned	Percent of Total
Premium and Other Taxes	2.1	11
Commissions	14.0	75
Agent Service and Promotion	1.5	8
Allocated General Administration	1.0	6
Total	18.6%	100%

Commission paid to agents is the most significant element of cost and represents about 75% of the total costs of this function. The 14% figure represents the ratio of the total dollar value of commissions paid by the industry to the total dollar value of premiums earned from automobile insurance.

The Committee has had the opportunity to consider the results from a recent Agency Study sponsored by the Independent Insurance Agents and Brokers of Ontario. An analysis of published data from this study is provided in Appendix L. In reviewing this information, it is apparent to the Committee that the agency system was able to earn a reasonable level of return on investment based on the 1976-1977 commission rate structure for automobile insurance lines. It would appear from the study that comfortable profit margins on automobile commission income can be maintained by the agency system, given a level of efficiency above the average. This would suggest to the Committee that there might be opportunities in the future to achieve reductions in the commission rate level if programmes to promote

efficiency could be developed across the entire agency structure. Conversely, improvement of overall systems efficiency might alleviate pressure on the insurers with respect to the level of commission rates.

In addition, in its study of government ownership, the Committee learned that the commissions paid by I.C.B.C. have averaged 8% of total revenues over the 1974-1976 period, compared to an industry average of 14% of premiums earned in Ontario. This wide difference in commission expense costs between Ontario and British Columbia appears to have been made possible in British Columbia by the reorganization to a substantially different and more efficient delivery system. It has also been suggested to the Committee that a justification for at least part of this difference is the provision of more individual service to the public by private insurers. In other words, a reduction in selling costs may not always be in the interests of the consumer if it results in a loss of a necessary service, such as explaining the product to permit the customer to make an intelligent purchase suited to his needs. Nevertheless, the Committee is convinced that there is an opportunity in Ontario to move towards a more efficient marketing system particularly in the provision of compulsory insurance.

The agency system has already shown its willingness to make improvements. Although the I.I.A.B.O. study was undertaken among other reasons to provide updated information on the cost of operating an agency, the study has also provided a useful management tool which agencies can use to plan and monitor their performance and, as a result, to improve the efficiency of their operations. The I.I.A.B.O. appears to be addressing the problem of efficiency with their Agency Study and other management training and development programmes. The Committee strongly encourages the agency system to develop further such programmes to promote efficiency.

The Committee maintains that, with the implementation of compulsory insurance in this Province, both the insurance companies and the agency network must strive to improve systems and procedures, to eliminate redundancies, and to improve management processes by utilizing the administrative, training and development and other facilities in their respective trade associations. Generally, the Committee encourages all segments of the industry to do all that is necessary to ensure that productivity keeps pace with market demands.

At the same time, from its review of both the insurance product and the methods of marketing under government ownership, it would appear to the Committee that the marketing function for compulsory insurance can be simplified under a plate-to-owner system of vehicle registration. Further simplification of the acquisition function would probably require the introduction of standard non-cancellable policies and a uniform classification system. These programmes would increase the convenience of buying compulsory coverage and would permit streamlining of the services performed by the agency system.

It is the Committee's recommendation that the industry examine ways of improving the efficiency of marketing the compulsory insurance product. The Committee expects that improved efficiency will permit an eventual lowering of the commission rate on compulsory coverage or at least will prevent substantial future escalations by controlling costs.

B. UNDERWRITING AND POLICY PROCESSING

As outlined in Chapter 12, the total estimated costs of the underwriting and policy processing function are as follows:

	Percent of Premiums Earned	Percent of Total
Direct Administration	5.5	69
Allocated General Administration	2.5	31
Total	8.0%	100%

Aside from pure administration costs, the most significant element of cost in this function relates to underwriting and the risk selection process. Without major changes to the present classification system and underwriting methods, it is difficult for the Committee to see how major savings or improvements could be achieved in this function.

It is possible to conclude that unless dramatic alterations are made to underwriting, or unless the rating structure is simplified as in Manitoba and Saskatchewan, the potential for improvement in this function is not significant. For example, I.C.B.C., a government insurance corporation whose rating and classification system most closely approximates that of Ontario, experiences an estimated 6.3% cost in this function. Conceivably, the 1.7% saving over Ontario relates primarily to the economies of scale in administration resulting from the I.C.B.C. monopoly. The Committee comments on its conclusions with respect to changes in the classification system in Part V of this Report.

Over the longer term, the Committee would expect that the implementation of compulsory insurance, as recommended by the Committee, would impact on the insurers' policy processing and underwriting costs for compulsory coverage. Policies might be eliminated and the contract made non-cancellable, thereby minimizing activity between renewal dates. The Committee also recognizes that the further step of simplifying the classification and rating system for compulsory coverage could result in some measure of longer-term savings in the underwriting process.

As far as pure administrative tasks are concerned, such as the issuing of policies, policy amendments, communication with insureds, filing, and related procedures, it is the Committee's impression that traditionally the industry has not been known to change quickly and take advantage of new technology.

However, the Committee has learned that, in recent years, many improvements have been made by the industry which serve to strengthen the management process and its ability to control costs and streamline the administrative systems. The I.B.C. Expense Allocation and Reporting System referred to in Chapter 12 is one example. Another example is the Policy Management System (P.M.S.) which was developed in the United States and appears to be gaining in acceptance and popularity in Canada in that 18 P.M.S. packages have been sold in Canada and are in the process of implementation. P.M.S. is a computerized on-line system for property and casualty insurance which rates and issues most policies; handles accounting, statistical, underwriting, claims, and billing systems; and produces marketing and management reports. It would appear that significant reductions in per unit costs could be ultimately achieved from the use of such a system.

The Committee wishes to emphasize the need for continuous improvement in administrative efficiency as a means of curtailing the escalation of premiums. **The Committee strongly encourages** the industry to place emphasis on the search for new technology and on the utilization of the present technology.

C. CLAIMS ADJUSTING

As outlined in Chapter 12, total costs for the claims adjusting function have been estimated as follows:

	Percent of Premiums Earned	Percent of Total
Adjusting Costs Charged Directly to the Claim File	11.0	73
Direct Administration	2.6	17
Allocated General Administration	1.5	10
Total	15.1%	100%

The most significant elements of cost in this function encompass those direct costs for legal, towing, independent and staff adjusting, and appraisal services which are charged directly to the claim file. These are the costs on which it is the most difficult to obtain any meaningful and factual statistics. The industry has been concerned about the escalation of these costs and has recommended new "Claims Reporting Allocation" principles, which were implemented early in 1977 and should provide the industry and the Superintendent's Office with better information on claims costs in the future.

Based on a comparison with the operations of the government insurers, outlined in the Committee's background study on "Government Ownership of Automobile Insurance", substantial potential for improvement appears to exist in the claims adjusting process. With the introduction

of I.B.C. sponsored Appraisal Centres, the industry has already initiated worthwhile improvements. At the present time, there are eight such facilities in Ontario and more are planned. However, the Committee believes there is significant potential for further improvement for two primary reasons:

1. I.B.C. Appraisal Centres are not uniformly promoted by all insurers. Insurers do not make the use of the Appraisal Centres mandatory to their policyholders, although most insurers will encourage their use by pointing out their advantages and the time savings realized.
2. I.B.C. Appraisal Centres only provide for one stop centralized appraisal; they do not provide for one stop claims adjusting.

As long as this separation of the adjusting and appraisal function is maintained, an opportunity for improvement in the claims adjusting function will not be realized.

In the course of its investigations in Regina and in Vancouver, the Committee was favourably impressed with the Claims Centres operated by S.G.I.O. and I.C.B.C. respectively. The benefits of this approach to claims settlement are several but can be summarized as follows:

- The elimination of the frustration, confusion, and inefficiency of a system involving numerous intermediaries, thereby increasing convenience to the public and increasing consumer understanding of the claims settlement process; and
- The curtailment of spiralling costs in the future by providing a centralized appraisal and adjusting mechanism that can exert effective control over repair costs and over negotiations for award settlements.

The Committee accordingly recommends that the insurance industry be encouraged to undertake a feasibility study of the mechanism that would be required to incorporate independent on-site adjusting in an industry Claims Centre in order to provide one stop appraisal and adjusting.

In the meantime, the establishment of further drive-in Appraisal Centres, as already initiated by the I.B.C., should be undertaken, until methods of incorporating the adjusting function are investigated. A practical method of funding and cost sharing among all companies, and not just members of I.B.C., should also be investigated. The Committee considers that all companies should bear their share of the cost of developing and publicizing Appraisal Centres and eventually, if feasible, Claims Centres. Policyholders should not be charged a user fee for use of these Centres and should be informed that they are free to seek appraisal and adjusting services elsewhere, if a drive-in centre is not located within a convenient distance.

Potential for improvement in the claims adjusting process can also be sought by examining the adversary system. For example, a reduction in administrative and adjusting costs appears to be achieved under a government ownership system in that the "one company" concept of government ownership eliminates much of the adversary problem. However, it would appear to the Committee that the most effective way to eliminate the costs inherent with the present adversary system is through introduction of some form of no-fault or modified no-fault system of compensation. Accordingly, the Committee has proposed in Part II of this Report certain fundamental changes to the system of accident compensation in this Province.

However, as long as the adversary system continues, **it is the Committee's recommendation** that the industry be encouraged to adopt methods of settlement that facilitate improved efficiency in paying third-party claims.

In addition, as long as the adversary system continues, increased public disclosure of the legal and adjusting costs associated with the adversary system is the only method of monitoring and controlling these costs. Therefore, **the Committee recommends** that the industry be encouraged to provide public disclosure of its legal and adjusting costs either through the I.B.C. or through the Superintendent's Office.

Certain of the costs of the adversary system, such as a claimant's legal expenses, fall outside the control of the insurance industry. Accordingly, **the Committee addresses the following recommendations** to the Ethics and Public Relations Committees of the Law Society of Upper Canada and the Advocates Society of Ontario regarding their public interest responsibilities:

- It is imperative that vigilance be maintained to discourage any practices involving the use of contingent fees.
- Adequate and full disclosure of estimated fees and disbursements should be provided by all legal practitioners prior to acting for the public in claims settlement matters.
- A liaison between these associations and the Superintendent's Office should be established to develop an appropriate form of monitoring the legal costs of claims settlement from the claimant's point of view. Legal fees and disbursements paid directly by claimants are presently subject to the standards and regulations of the Law Society of Upper Canada and fall outside the present insurance regulatory process. Yet these costs represent a substantial cost inherent in the existing system of claims settlement. The Committee encourages the Law Society of Upper Canada, as a self-regulating professional body, to undertake a study, on behalf of the public it serves, to determine the costs incurred by claimants in the procurement of legal advice regarding the matter of auto insurance claims.

D. EXPENSE LOADING

In determining its premium requirements, an insurer determines its own loss experience and "adds" a margin to cover its operating expense estimates, profit requirements, and other such factors. If an insurer does not have the in-house capability to do this, it may utilize the rates prepared by I.A.O. Alternatively, it may use I.A.O. rates in the first instance and then deviate from them based upon its own loss and expense experience. In effect premium requirements are distributed across the various rating categories during the rate setting process by the use of statistically developed "differentials".

By applying a percentage add-on to cover expenses, it is entirely possible and likely that certain rating categories and risk classifications will bear a disproportionate share of expense costs and, to this extent, rates in these classes may be unfair or inequitable. A potential safeguard against this situation, short of rate setting by a government department or agency, or by a government corporation, is a market place which fosters competition, provides for full and adequate consumer knowledge, and encourages consumers to shop around.

Operating expenses and loss costs differ by insurer and, even with the implementation of a uniform classification system, individual rates would continue to reflect individual levels of efficiency. The Committee recognizes that it is not practical and likely impossible to develop a system which would accurately allocate actual costs to various types of coverage, various rating categories, or various deductible limits. The cost of such a system would certainly not justify the benefits to be derived from it. It might be practical however, to separate the expense loading factor into its main fixed and variable components, allocate a standard or fixed cost to all policies and then apply variable costs in proportion to the level of work involved on the policy. Some insurers already follow this practice in a simplistic fashion and, accordingly, their rates reflect a more equitable premium for each category of insured. For example, one insurer charges a separate "write-up" fee for the first policy, with a reduced expense loading factor applied to policy renewals.

The potential inequity of the present method of expense loading was brought to the Committee's attention during its investigations in Florida and Massachusetts. The problem, as identified in these states, can be explained as follows:

"The traditional practice of loading commissions and other expenses of doing business (not including claims adjustment expenses, premium taxes and profit allowances) into the premiums by an across-the-board percentage produces great inequities among policyholders of different classes. If we assume 25% of the premium goes for such expenses, then a young driver in an urban territory whose premium is

\$1,000 pays \$250 in expense dollars whereas a senior citizen in a rural territory with a premium of \$200 for the same coverage will have only \$50 in expense loadings to pay. It seems reasonable to assume that it doesn't cost the agent and company five times as much to do business with the youthful driver, remembering that claims adjustment expenses are not included in this expense item¹.

The insurance industry in Massachusetts has itself admitted the need to equalize at least some of their expenses. In the recent rate filings before the Insurance Commissioner, the industry agreed to even out the allocation of most company expenses, with the exception of commission and Facility expenses. There are, however, moves underway to extend the equalization of company overhead expenses to all policyholders including those in the Facility.

In Florida, recommendations have been put forward by the Grand Jury investigating automobile insurance rates in Dade County to apply the equalization of expenses to all policyholders including those in the Florida Joint Underwriting Association, and to include commission expenses in the equalization process. The Grand Jury's recommendations are in this regard as follows:²

"The Insurance Commissioner should immediately order all insurance companies doing business in the State of Florida to cease calculating expense loading as a percentage of premium. Company expenses should be pro-rated as a fixed dollar amount against all policies issued. If any company expenses can be proven to vary by location, allowance should be made therefor.

Agents' commissions should be based on a fixed amount per policy issued, which would be a flat dollar amount statewide, plus a nominal percentage of the premium to cover differential cost of agents doing business in various parts of the State."

The objective of these recommendations was to equalize each individual policyholder's contribution so that he pays only his fair share of the insurance company's sales and administrative expense.

The Committee is equally concerned about the present practice of expense loading in this Province and strongly encourages the industry in Ontario to undertake a more equitable method of allocating and distributing expenses. **The Committee recommends** that the industry begin immediately to investigate procedures whereby costs can be applied in proportion to the level of work involved on a policy.

1. National Association of Insurance Commissioners, Discussion Paper, Zone 1 Meeting, Boston, Massachusetts, September 19, 1977.

2. Dade County Grand Jury, "Investigation into Automobile Insurance Rates", January 5, 1978, Florida.

The Committee further recommends that the industry provide the Superintendent with the results of its investigations and continue to provide relevant expense data compiled under industry reporting systems, such as the I.B.C. "Expense Allocation and Reporting System". This information should be assessed by the Superintendent with the intention that he issue at the end of five years time a report indicating the progress, or lack of progress, of the industry in developing a more equitable expense loading system.

PART V

THE RATING CLASSIFICATION SYSTEM

CHAPTER 14

The Present Rating Classification System in Ontario

A. INTRODUCTION

During its deliberations leading to the preparation of its First Report, the Committee reviewed in considerable detail the methods used by the insurance industry to set automobile insurance premiums¹ and identified a number of concerns related to:

- The need for a classification system that is entirely objective and actuarially sound. Certain aspects of the present classification system appear to be arbitrary or subjective.
- The need for a clear and understandable system of classification, a condition which is not apparent given the large number of classes in the present system.
- The need for the calculation of premiums to be based on a set of objective, clear and understandable criteria.

Subsequent to its First Report, the Committee has had the opportunity to learn about classification systems used or proposed in a number of other jurisdictions. In addition, further information from the Committee's consultants and from the Superintendent's Office on the subject of a standardized rating classification system have assisted the Committee in reaching conclusions on this topic.

In this chapter, the Committee considers further matters related to the present system of rating in Ontario, followed in the next two chapters with the Committee's conclusions regarding the need for improvements in the classification system. The Committee recognizes that the matter of the "actuarial validity" of a system of rating is one on which qualified experts in the industry and in the Superintendent's Office will need to comment given the conclusions in this Report.

B. BACKGROUND

The following is a brief review of the major factors presently taken into account in rating in Ontario with particular emphasis on two matters: the degree of standardization, and the objectivity or statistical base of the various factors used.

The automobile first came into prominence in the United States and it was there that the need for automobile insurance was first recognized. There may have been a time, in the infancy of automobile insurance, when

1. The Select Committee on Company Law, *The Insurance Industry—First Report on Automobile Insurance*, Province of Ontario Legislative Assembly, 1977, Part III, pages 87-113.

the total premium requirements for a period were divided among the number of drivers to establish an average premium that all would pay. The first principle of automobile insurance, that the premiums of the many would go to pay the losses of the few, would have been satisfied. Regardless of whether this practice was ever followed, it was soon recognized that there was a second "principle" of insurance ratemaking, that the premiums charged to insureds should vary according to the degree of risk or hazard they imposed on the insurance system. In their judgement at the time, those responsible for determining automobile insurance premiums decided that the first differentiation of drivers, and hence the first rating classification, would be based on whether an insured's vehicle was used for business purposes or solely for pleasure.

Not long after, an additional classification system was added that differentiated for ratemaking purposes between under 25 and over 25 year old drivers. Some time later, a rating classification differentiating between male and female drivers was established. Still later, the under 25 age category was subdivided into those 16 to 18 years of age and those 18 to 24 years of age. In this fashion, by evolution, the present classification system as used for ratemaking purposes in Ontario was developed.

At the time that they were introduced, the selected classifications were ones that were "socially" acceptable and ones which "everyone would acknowledge were reasonable". It is possible to speculate that different classification systems might have developed if different social, economic and political philosophies had been popular when rating classification began.

As various methods of establishing classifications for automobile insurance rating purposes were established, compatible statistical data of claims experience for each classification were developed to compare claims costs with premium revenues. While the establishment of a specific classification system did not preclude the development of other statistical data and the possibility of other methods of rating, the main thrust of any organized approach by the industry to developing information was dictated by the classification system generally in use. Individual companies on occasion have indicated initiative in trying to establish modifications to the existing classification system; but there has been no continuing programme by the industry as a whole, or by major segments of it, to evaluate and reassess the system in use in an effort to determine whether better bases and methods of classification might be more appropriate and practical.

In Canada a standardized format for accumulating statistical information concerning automobile insurance premiums and claims costs has been developed. Superintendents of Insurance of all of the Provinces except British Columbia, Saskatchewan and Manitoba have agreed to have a statistical agency gather information concerning automobile insurance pre-

miums and claims. Since January 1969, this statistical agency has been the Statistics Division of the Insurance Bureau of Canada. The statistical information that is to be provided to the I.B.C. is set out in the Statistical Plan. This plan calls for each company to report information each month on each policy written or cancelled and on each payment on a claim, in effect on every transaction concerning every policy. In addition, other data including information concerning outstanding claims must be reported at specified times during the year. All of the information is then compiled by the Statistical Division of the I.B.C. and published annually in the "Green Book".

C. REVIEW OF THE PRESENT RATING FACTORS

Data concerning the date each policy is written and its term are reported to the Statistical Division of the I.B.C. In addition, a number of other factors that are used in rate determination are also reported, including:

- the area where the policyholder resides,
- the age of the operator and the use to which the vehicle is put,
- the accident (not the conviction) record of the driver,
- the limit on third-party liability coverage purchased,
- the deductibles on own-vehicle coverage purchased,
- the value of the insured's vehicle.

These latter factors are not applied in a consistent fashion by all companies in the rating of drivers. Outlined below are brief comments on the manner in which the actual factors used by the industry are applied in determining premiums in relation to those factors on which there are reported data.

1. *Geographical territories*

The Statistical Plan divides Ontario into nineteen statistical territories. For rating purposes some of the smaller territories with characteristics in common are combined so that there are only twelve rating territories in general use by insurers in Ontario. While all insurers in the Province report to the Statistical Division of the I.B.C. on the basis of the nineteen territories as defined in the Statistical Plan, the territories they use in the preparation of their rate manuals do not always conform with the standard territory boundaries.

2. *The age of the operator and the use to which the vehicle is put.*

The Statistical Plan categorizes all drivers into fourteen separate groups depending upon their age and the use to which their vehicles are put. Once again all companies conform with the requirements to report according to the Statistical Plan categories. However, the rate manuals used by some companies differ from the categories in the Statistical

Plan and these companies therefore find it necessary to "force" the information they report to meet the requirements of the Statistical Plan. Such practices could distort the "objectivity" of the loss cost reports based on these data.

3. *The accident record of the driver.*

The Statistical Plan rates drivers in five categories depending upon their accident record ranging from those who have had an accident within one year to those who have had five accident-free years. However, the practice followed by individual companies in implementing this category structure in the rates they charge their policyholders, differ widely. While there is no consistency in the practices followed by the industry, all insurers are able to rationalize their particular practices with the standard definition and to report as required to the Statistical Division of the I.B.C. in keeping with the requirements of the Statistical Plan. This appears to indicate that rating based on accident record is not always applied objectively by all insurers.

4. *The limit on third-party liability coverage.*

Historically, third-party liability policies have been issued with limits ranging from \$35,000 to \$1,000,000. However, in the past, the Statistical Plan has required only that all transactions be reported for policy limits up to \$200,000. It was only in June 1977 that the Statistical Plan was amended to require that companies report transactions on policies for \$300,000, \$500,000 and all policies with higher limits than \$500,000. It will take a number of years for credible statistics to be developed to reflect the experience on \$300,000 and \$500,000 policies. In the meantime premium rates for policies with limits in excess of \$200,000 will continue to be quoted by insurers based on "add-ons", with each company deciding, based on its own subjective assessment, the differential in premiums needed to cover the higher limits.

5. *The deductible on own-vehicle coverage.*

There is general consistency in the deductible limits quoted by most insurers and in the method of reporting information concerning collision and comprehensive policies as set out in the Statistical Plan. No separate statistics are developed for Ontario concerning deductible limits for these coverages. Rather, these data are developed on a country-wide basis, excluding British Columbia, Saskatchewan and Manitoba.

6. *The value of the insured's vehicle.*

No objective statistical data are accumulated on an industry-wide basis to support differentials in rates that are charged to policyholders on the

basis of the value of their vehicles. As a consequence, it can be said that premium rates related to the value of an insured's vehicle are determined by the individual companies, based on their own assessment of appropriate rates in the light of their own experience and in the light of the rates quoted by their competitors.

In addition to the above variations within reported rate categories, there are many other variations in the methods used by individual companies to determine the rates they are prepared to quote their customers. There may or may not be consistent statistical data within these companies to support the rates charged. As examples, some companies are prepared to give discounts to "good-students"; others are prepared to give discounts to abstainers. Rather than using the driving record as a basis of rating, one company uses a claim service fee which is charged to a claimant in the case of an accident. In general, there is no consistency in the number of vehicle rating groups that are used by companies; most use eight rating groups, although many use several more. Further, some companies maintain a car in the same rating group for its life, while others provide that as a vehicle gets older it moves to a lower premium group for rating purposes.

The Committee has been informed that the extent of the deviations from "standard" in the practices followed by individual companies is one of the subjects currently being reviewed jointly by representatives of the Superintendent's Office and the industry. The Superintendent's Office has requested data from insurers writing automobile insurance in the Province in an effort to ascertain more precisely the nature and extent of the variations in the classification systems followed in the preparation of rate manuals. On the basis of preliminary discussions with industry representatives it is apparent that, while there is a framework for standardization of rate categories in the Statistical Plan, significant variations exist in practice.

D. CONCERNS ABOUT THE PRESENT CLASSIFICATION SYSTEM

The variations observed in the present classification system are of concern to the Committee in that some companies may be applying rating factors on which there may not be sufficient or accurate loss experience data. As a result, rates may be arbitrary or not adequately objective. This raises the concern that the premium burden borne by policyholders for certain coverages or in certain rating categories may not be fair and equitable; however, lack of appropriate statistical data often makes such a determination impossible at the present time.

The extent of variations in the classification systems used by individual insurers is of further concern to the Committee for the following primary reason: it is the Committee's view that the insured, under the present

system, frequently is unable to "price-shop" because of confusion about the insurance product and confusion about the manner in which prices are determined.

In many ways the buying process for automobile insurance is similar to that of buying most other products. The "insurance product" can be defined by type of coverage and coverage limits, and the existence of a standard automobile policy sets terms which are applicable to all parties. Without knowing all the factors that make up price, a buyer can approach numerous insurers or agents until he is satisfied that he has found a "good" price for the insurance product he wishes to buy. As in the case of the purchase of many other products, price need not be the sole determining factor in the choice of an insurer; service or reputation may also influence the buyer's choice.

Nevertheless, "price-shopping" for insurance appears to differ from buying most other products in several ways:

1. Some sellers may be unwilling to sell their product to certain buyers;
2. The price each buyer will pay, and his ability to purchase in some cases, is affected by the buyer's characteristics;
3. Each insurer may "assess" each buyer's characteristics in a different way to arrive at the price of the insurance product;
4. The price to the buyer will likely change as his characteristics change. The buyer is generally unaware of the extent to which his premium will vary with a change in his status as he is usually unaware of the rating factors that each insurer applies in arriving at either the original or revised rate;
5. Time is a component of the insurance product and its price. The product is sold for a limited period of time, often one year, and must be repurchased for continual coverage. Some sellers may be unwilling to sell to certain buyers except for short periods of coverage or may be unwilling to renew coverage at some point in the future.

It is the Committee's view that, because the vehicle owner influences the price he pays for insurance coverage, he has a right to understand *how* he influences the price. This understanding would likely act as an incentive for better driving and fewer claims. At the same time it would facilitate and perhaps encourage price-shopping.

It is the Committee's strong conviction that the numerous classification systems presently in use do not permit an understanding by the insured of the characteristics used to determine the rating group into which he falls and the price he must pay.

In this regard, the Committee commented as follows in its First Report:

“The principal criterion for a proposed new classification system will be its complete objectivity. It is the Committee’s intention that the present underwriting practice of taking various subjective factors into consideration in deciding whether to write a policy should be abolished. An applicant should then be judged on the basis only of the authorized criteria and he will be entitled to have his premium calculated accordingly and to be insured upon payment of that premium.”¹

In light of the Committee’s recommendation that third-party liability insurance be made compulsory in the Province, the Committee continues to be convinced that the present rating procedures and practices should be improved from the insured’s point of view.

1. Select Committee on Company Law, *First Report on Automobile Insurance*, page 124.

CHAPTER 15

Standardizing The Rating Classification System

In the previous chapter, the Committee stated its strong conviction that the present rating procedures and practices do not permit an understanding by the insured of the characteristics used to determine the price he must pay for the insurance product, and therefore these rating practices should be improved from the insureds' point of view. Accordingly, **the Committee recommends the establishment of a mandatory basic rating classification system**, with which all insurers selling automobile insurance in the Province would comply, as a constructive method of ensuring that a vehicle owner can price-shop for his insurance.

The Committee envisages that the recommended mandatory standard classification system would embody the following features.

1. Of necessity, such a classification system would be based initially on the general criteria presently used in the Province for rating purposes. Standardization of this structure would permit ready identification of the "cells" into which an individual insurance buyer would fall. Each company would then be required to establish rates for each cell or segment of the market place to which it is prepared to sell.

The structure making up the classification system should be designed around mandatory definitions of the factors to be taken into account in rating, for example, at present:

- the rating territories,
 - the age of the operator and the use to which the vehicle is put,
 - the accident record of the driver,
 - the limit on third-party liability coverage,
 - the deductibles on own-vehicle coverage, and
 - the value of the insured's vehicle.
2. The driving public must be made aware of the factors taken into account in determining premium rates and the basic definitions of the mandatory classification system. In order to ensure that the drivers are given an opportunity to understand the manner in which their premiums are determined, the factors taken into account in determining their "cell" for rating purposes should be noted in straightforward language, rather than by codes, on all applications for insurance, insurance policies and insurance renewal notices.

In general, under either the present system or under a standard classification system, **the Committee recommends** that the industry be required in legislation to inform all policyholders of the criteria used by the insurer to classify the vehicle owner to a particular rate category. Disclo-

sure of the criteria should be in writing and should form part of the policy application and all related forms.

3. **The Committee recommends** that all reporting of policy transactions under the Statistical Plan be made on the bases of the mandatory classification system. In this way all data concerning basic categories would be objectively and statistically supported as data would be reported and accumulated for all transactions on consistent and universal bases to conform with the mandatory classification factors, as defined,
4. The Committee recognizes the potential inflexibility of standardized rate classes. The Committee also recognizes and indeed anticipates that there are likely to be pressures to introduce new insurance concepts in the Province. Further, the Committee is concerned that the industry's ability to introduce new ideas could be inhibited with standardization. For these reasons the Committee considers that the potential rigidity of a mandatory standard classification system should be modified in the following regard.

To accommodate the orderly introduction of new concepts of insurance in the Province, it is necessary to establish a mechanism for introducing new classification "cells". **The Committee recommends** that the establishment of new rating groups or coverages should be subject to the prior approval of the Superintendent's Office.

As new concepts are introduced it is probable that there will be insufficient data on which to develop objective rates. For example, in the past, third-party liability policies were sold with limits in excess of \$200,000 although data were not required to be reported separately for higher limits until a change was made in the Statistical Plan in June 1977. If it were decided to set new policy limits or introduce new rating groups, the range of premiums to be charged by individual companies would likely be related in some fashion to rates being quoted for standard rate classes. If the new rating groups or coverages receive the approval of the Superintendent's Office, amendments should be made to the Statistical Plan to require the separate reporting of policy transactions for these new groups or coverages so that objective and statistically based experience data could be developed and in time become part of the mandatory basic classification system.

CHAPTER 16

Discrimination In Rating

A. INTRODUCTION

As noted in Chapter 14, the factors taken into account in the rating classification system presently in general use in Ontario have developed by evolution from "socially" acceptable classifications of vehicle owners and drivers dating back in many instances forty or fifty years. In dealing with the need for standardizing rating classifications in the Province, the Committee's conclusions and recommendations in Chapter 15 have been made without regard to the specific rating classification criteria used by the industry. Nonetheless, the Committee considers the proposals in Chapter 15 to be relevant whether the factors taken into account in rating for insurance purposes remain as at present or are changed to embody new criteria in years to come.

The Committee has been concerned, however, with a number of matters relating to the factors presently used in rating vehicle owners and drivers for automobile insurance. In particular, the Committee is concerned that many of the factors discriminate against certain groups of the driving public. During its review of the subject, the Committee learned that it was not alone in its concern and that other jurisdictions have considered the subject of discrimination in rating. In particular, the Committee had an opportunity to review in some detail the methods of rating adopted in Saskatchewan and Manitoba in Canada and the studies and current developments in Massachusetts and Florida in the United States.

B. BACKGROUND

The following comments highlight the main features of the practices either in use or proposed in several jurisdictions.

Manitoba and Saskatchewan

The rating classification systems for compulsory insurance coverage in Saskatchewan and for compulsory and extension insurance coverage in Manitoba have both been simplified to include only relatively simple and broadly defined rating factors. More "traditional" factors continue to be used for rating purposes for extension coverage in Saskatchewan.

The distribution of the total income requirements of the government insurance corporations among various sources of income is determined in relation to the rating factors that make up the classification system. The sources of income of the government insurers in Saskatchewan and Manitoba are dealt with in some detail in the Committee's background study on "Government Ownership of Automobile Insurance". Briefly, they consist

of investment income and "premium income" from these sources—certificate of insurance premiums, drivers' licence fees, and gasoline tax. These sources of premium income are related to rating for basic coverage in Saskatchewan and for both basic and extension coverage in Manitoba on the basis of the following simple facts:

<i>Rating Factor</i>	<i>Income Source</i>
— The use of the vehicle	— gasoline tax and basic drivers' licence fees.
— Value of vehicle	— certificate of insurance premiums.
— Driving record	— demerit point surcharges as part of the drivers' licence fee.

Neither Province uses age, sex, marital status or the occupation of the vehicle owner or driver as criteria in their rating classification system. Further, Saskatchewan has eliminated territorial rating, while Manitoba has four rating territories. Manitoba also has four classes of vehicle use—preferred, all-purpose, farmer, and business—used to differentiate premiums charged for the certificate of insurance.

Florida

During its hearings in Florida, the Committee met with several interested parties to review and discuss the results of studies and hearings on automobile insurance rating in that state.

The main concern of those who appeared before the Committee was that those most likely to be overcharged for automobile insurance were those least able to afford it, including motorists who happen to reside in urban areas, to be young, to be poor, or to be members of minority groups. It was acknowledged that all of the problems of overcharging could not be related solely to the rating classification system. For example, the method of expense loading as used by the industry, to which further reference has been made in Chapter 13 of Part IV of this Report, and the particular problems of the residual market in Florida were also contributing factors. Nevertheless, the impact of the rating system was considered to be very significant.

The conclusions of the Grand Jury in Dade County carrying out an investigation into automobile insurance rates was that many of the classifications used in determining premiums were discriminatory. The Jury expressed the view that the only acceptable system of classification is one based on factors within an individual's control and on those factors that are actually related to causing losses. Among its recommendations, the Grand Jury included in its final report filed January 5, 1978 the following:

- "1. Insurance companies should be prohibited by law from using sex, age, or marital status as a classification in determining the premiums

to be charged an individual motorist. Driver classifications should be restricted to the following:

- A. Drivers with less than three years driving experience.
 - B. Drivers with more than three years driving experience.
 - D. Business use.
 - D. Annual mileage driven if it can be accurately verified.
4. The Insurance Department should institute an immediate study in order to determine the effect of eliminating geographical location as a factor in establishing insurance rates.
 7. The Insurance Commissioner should immediately order all insurance companies doing business in the State of Florida to cease calculating expense loading as a percentage of premium. Company expenses should be pro-rated as a fixed dollar amount against all policies issued. If any company expenses can be proven to vary by location, allowance should be made therefor.
 8. Agents' commission should be based on a fixed amount per policy issued, which would be a flat dollar amount statewide, plus a nominal percentage of the premium to cover differential cost of agents doing business in various parts of the State.
 14. The Insurance Department should immediately study alternative means of handling the substandard insurance market, including a reinsurance facility in which the rates would be the same as any participating company's voluntary market. The system which best serves the public interest is the one that ought to be placed in use in this State, regardless of the preferences of the insurance companies."

Massachusetts

Likewise, during its hearings in Massachusetts the Committee was appraised of some of the studies that had been undertaken in that state and the resulting conclusions and recommendations including:

- "3. The current classification system, which varies insurance rates primarily on the basis of age, sex and geography, should be replaced with a system that relies primarily on the individual's driving record. The current system is arbitrary, inaccurate and discriminatory. It leads to overcharges of many good drivers and provides no incentive for better driving and fewer claims.
4. The rate-making formula should be changed to include a "density factor" for each territory to reflect the impact of traffic from surrounding areas.
5. All policyholders should bear an equal share of the insurance companies' overhead expenses. At present, drivers with the highest bills bear a much heavier share of industry expenses. Recommendations 3,

- 4, and 5, coupled with the general decrease, could lower premiums for some hard-pressed urban and young drivers by 15 to 30 percent.
8. Rates should be set in such a way that they will continue to create an incentive for motorists to reduce losses and for companies to develop programs to reduce fraudulent claims."¹

In Massachusetts, the Commissioner of Insurance has the power to set insurance rates. In determining the rates the industry may charge in 1978, he has eliminated age, sex and marital status as factors to be taken into account and instead has created two new classes of motorists—those “with” and those “without” three years of driving experience. The Commissioner further ordered that the difference in rates between city, suburban and rural areas be lessened.

Other States

In addition to Massachusetts and Florida, the Committee understands that the state insurance departments in New York and Illinois are studying a variety of proposals to reform the criteria used for classification purposes in determining automobile insurance premiums.

Steps toward reform are being initiated in California by way of court action commenced by Los Angeles County for “discovery rights” to insurance company data on the County’s vehicles in order to assess the validity of territorial rating procedures. In Los Angeles County there is an extreme variation in rates (up to 10 times higher in some territories) charged to vehicle owners residing in the city of Los Angeles and in the surrounding rural areas. County supervisors feel the loss experience in the city is caused by commuting traffic and therefore that rates should be averaged over a broad territory including the city and outlying areas.

The Committee also understands that in New Jersey the state insurance department is involved in detailed consideration of reforming the automobile insurance rating classification system.

North Carolina presently prohibits classification by age and sex.

C. CONCERNS WITH THE PRESENT CLASSIFICATION SYSTEM

Any review of the traditional ways of calculating insurance rates has its focus on the relative burden of the insurance system to be borne by vehicle owners and drivers in differing rating categories. Any such assessment leads to such matters as:

- Should driver experience replace age, sex and marital status as a rating classification criterion?

1. Massachusetts Fair Share, Inc., “Stop Highway Robbery: The Fair Share Plan for Lower Automobile Insurance Rates”, September, 1977.

- Should a driver's driving record be a factor taken into account in some fashion in determining insurance premiums?
- Is there validity to a multitude of rating territories?
- What is the appropriate balance between social and actuarial considerations in ratemaking?

All those jurisdictions that are in the process of reforming the traditional rating classification system appear to be striving to replace age, sex, marital status and additionally in some jurisdictions geography, with driver experience and driving record as more appropriate classification criteria.

Throughout their studies, various groups have expressed their concern that the current classification scheme provides no incentive for an individual to change behaviour patterns, since risk is, in many instances, being assigned not on factors over which an individual has control but on group characteristics such as age, sex and geography. This has led to the view that the industry should move towards an insurance system which places greater reliance on individual driving records rather than on group characteristics. It is argued that a system based on driving merit is fair and equitable and that such a system is clearer and more objective than the current classification system, and that it will give motorists a real incentive to drive carefully.

Another study provided to the Committee expressed the view that the accident differentials between young males and females may be related to the number of miles driven, assuming that "males drive much more than females do". Thus, it is suggested that sex may be a surrogate for miles driven and is used because it is more convenient to measure. This same study also suggested that age has been viewed as a good predictor of accident likelihood not necessarily because young drivers are more careless but because age is a conveniently measured surrogate for driving experience. This study then expressed its concluding view that driving experience, which may be estimated by the number of years licenced, is an alternative and perhaps more appropriate classification technique which, to a certain extent at least, is within the control of a driver.

D. CONCLUSIONS

The Committee recognizes the need for an appropriate rating classification system if the second principle of insurance ratemaking is to be satisfied—that the premiums charged to individuals should vary according to the degree of risk or hazard they impose on the system. According to this principle, a classification system should be designed to establish a statistically accurate manner of determining expected losses from insureds who are different risks so that the proper costs of providing the necessary coverage may be determined. However, the Committee is inclined to concur with the conclusions reached in the studies in Massachusetts and Florida that the present classification system is discriminatory and unfair by over-

charging those good drivers who might be members of a high risk class for reasons beyond their control.

The Committee's concern in this regard is compounded when it reviews the industry's traditional methods of expense loading and paying agents' commissions. In general, both expenses and commissions are calculated as percentage add-ons to a basic premium. To the extent that "discrimination in rating" results in penalizing certain classes of drivers, the premiums these drivers must pay are made even more unacceptable by the current expense loading practices.

In summary, **the Committee is impressed** with the arguments in favour of eliminating age, sex and marital status as criteria to be used in determining automobile insurance premiums, **and it urges** the industry and the Superintendent to develop alternative criteria. The Committee considers that more appropriate criteria would be driving experience, driving record, and miles travelled if an objective measurement of this latter factor could be found.

The Committee wishes to reiterate that it is greatly impressed with arguments in favour of a classification system that provides an incentive to individual drivers to drive more carefully and that rewards safe driving with lower insurance premiums. It is the Committee's view that "good-driving incentives" should be made particularly attractive to young drivers. The Committee encourages the industry and the Superintendent to give attention to this matter.

PART VI

SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

CHAPTER 17

Summary of Conclusions and Recommendations

The following is a summary of the conclusions and recommendations that the Committee has reached, as set out in this Report.

PART I: IMPLEMENTING COMPULSORY AUTOMOBILE INSURANCE

Chapter 1—Compliance with Compulsory Automobile Insurance

1. The Committee in its First Report recommended the implementation of compulsory automobile insurance in the Province.
2. While the necessity of third-party liability insurance for the vehicle owner has long been recognized and widely accepted in Ontario, coverage is at present voluntary. However, the uninsured vehicle owner must pay \$100 into the Motor Vehicle Accident Claims Fund or, alternatively, qualify as a "self-insurer".
3. At the present time proof of insurance at the time of vehicle registration is by self-certification.
4. Various sources have estimated that the total number of uninsured vehicles in the Province ranges between 7% and 12%, or on average 10%, of all registered vehicles.
5. The Committee is convinced that the basic requirement of an effective compulsory insurance system is that all vehicles must be insured and remain insured for as long as they are licenced. This requirement can be fulfilled as follows:
 - (a) All vehicles which require vehicle licences should be required to carry the minimum third-party liability insurance and Accident Benefits coverage.
 - (b) Private corporations and government bodies whose activities are substantially commercial should not be excluded from the requirement to provide proof of insurance for their motor vehicles.
 - (c) The present exemption for governments should be reviewed so that only federal and provincial government ministries, departments and agencies not engaged in commerce would be considered to be exempt from compulsory insurance. Municipalities should be required to provide proof of insurance.
 - (d) Exemption from the principle of compulsory automobile insurance should be granted to those religious groups able to demonstrate that it is against their fundamental religious conviction to rely upon the au-

tomobile insurance system. This exemption is conditional upon the applicants establishing that the losses which they occasion will be paid as fully as though they were insured under all compulsory forms of insurance.

6. The Committee is convinced that a system of compliance with compulsory automobile insurance can be developed in this Province that will be efficient and more effective than a system relying on self-certification reinforced by greater police enforcement. A *model* of an efficient compliance system would encompass the following salient factors:

- The present “plate-to-vehicle” system of vehicle registration would be replaced by a “plate-to-owner” system.
- Positive proof of the required insurance coverage would have to be provided to the licencing agent at the time of the vehicle permit (licence plate) issue or renewal.
- The expiration of the insurance policy for a vehicle would be coterminous with the expiry of its licence plate.
- In order to spread the work load more evenly throughout the year a system of staggered or cyclical renewals of licence plates during the year would be introduced.
- An insurance policy would be non-cancellable before its expiry date, by either the insurer or the insured without proof of replacement coverage or the return of the licence plate to which the insurance applied.

The introduction of such a system would however create some difficulties as described in this chapter and in the next. The general conclusion of the Committee regarding the *model* system is provided in Chapter 2.

The introduction of such a system would also require the cooperation of the insurance industry and of several Ministries of Government of the Province. In this regard, the Committee has been advised that a review of the vehicle registration system in Ontario is already underway by an Inter-Ministerial Committee consisting of senior representatives of the Ministries of the Attorney General, Consumer and Commercial Relations, the Solicitor General, and Transportation and Communication and while the precise status of work has not been made public, it has been indicated that the *model* system envisaged in this Report is compatible with their views. Further, the Committee has been assured of the traditional cooperation of the insurance industry to implement any control mechanism.

7. Regardless of the compliance procedures that are introduced, there will always be uninsured vehicles. Accordingly, provision should be made for significant minimum penalties for non-compliance. The penalty for not having insurance or falsifying insurance is suggested to be a mini-

imum of not less than twice the approximate cost of the insurance, and should include licence suspension.

8. The Committee has concluded that there is value in setting out clearly in the Insurance Act the specific authority for police to stop a vehicle for the purpose of checking for compulsory insurance coverage and recommends that the Minister make such changes to the Act.

Chapter 2—Some Implications of Compulsory Insurance and the Compliance System on the Operations of Insurers in the Province

1. In this chapter the Committee reviews some of the difficulties that would arise for both the insurers and the insureds with the implementation of compulsory insurance in the Province and the *model* system of compliance envisaged in Chapter 1.
2. While the industry has indicated that they would prefer, in general, to maintain the present compliance system by reinforcing self-certification, the Committee has been assured of the traditional cooperation of the insurance industry in implementing any control mechanism.
3. After reviewing the practicable aspects of a compulsory insurance system that incorporates the five points set out in Chapter 1 as a *model* system of compliance, the Committee has concluded, with the exception of the condition that follows, that such a system should be implemented in Ontario.

The Committee's recommendation is conditional on the requirement for further study in the area of alternatives to the irrevocable policy. However, should study into this matter indicate that a satisfactory integration of vehicle registration cancellation with insurance coverage cancellation cannot be established, the Committee is convinced that solutions to difficulties associated with non-cancellable policies can be found and that the irrevocable policy should be included as an integral part of the compliance system for compulsory insurance.

Chapter 3—Ensuring the Availability of Insurance to the Driver in Ontario

1. It is axiomatic that, when automobile insurance is made compulsory in the Province of Ontario, licenced drivers must be able to purchase the coverage they require easily. However, the Committee recognizes there are problems in fulfilling this requirement caused by the geography of the Province; by the capacity of individual insurance companies to write all of the automobile insurance that applicants may wish to place with them; by the desire of each company to select only the best risks for its account; and by many other factors.

2. The problems relating to the availability of insurance can be grouped under the following headings: marketing, or the alternative means by which an insured or his agent will have access to insurers; underwriting, relating to the matter of risk retention and the method of pooling undesirable risks; and rating, with specific reference to the premium rates to be charged to high risk drivers.
3. The Committee has reviewed the various methods of marketing insurance and concluded that a marketing system which denies the customer access to the insurer of his choice is unacceptable, particularly after the enactment of compulsory insurance. Accordingly, the Committee has decided to recommend that the automobile insurance industry adopt the take-all-comers principle in marketing compulsory insurance. This plan would serve the public of the Province best, by providing the customer with direct access to the insurer of his choice at the rate ordinarily charged by that insurer for the classification into which the insured falls.
4. The Committee recognizes that with the adoption of the take-all-comers system there is the potential for problems for individual insurers and the insurance industry as a whole. For example, any one company might be forced to write business beyond its capacity having in mind the solvency rules under which each company operates. Further, any company might be forced to write a disproportionate share of the high risk market in any one category.

For these reasons, the Committee concludes that the industry must be prepared to undertake 100% pooling of residual risks but should be free to determine the structure of the pooling mechanism required to implement the take-all-comers approach.

It is implicit in the foregoing two recommendations that the premium chargeable for high risk drivers should be the company's published rate for that risk and there must be no surcharging merely because the risk is pooled.

5. The Committee recognizes that the industry as a whole may not be enthusiastic about 100% pooling as a solution to the capacity problem of take-all-comers, since it is conceivable that through errors of judgement or miscalculations, an individual company might underprice the coverage in a particular category and yet be able to minimize its potential losses by transferring some of the consequences of its mistake to the rest of the industry through 100% pooling of the risk. Carried to its extreme, one portion of the driving public could be subsidized by all other drivers. With the adoption of 100% pooling as an alternative to risk retention, the Committee is persuaded that, as a minimum, procedures would have to be set up whereby the Superintendent of Insurance, either on his own or on the basis of complaints from within the industry, could investigate "bad faith" or grossly inadequate rates and have them corrected.

6. The Committee further recommends that the Superintendent of Insurance be given the right and the obligation to evaluate the operations of the 100% residual market pool and carry out analyses of its population. It is the intention of the Committee that the Superintendent monitor the operation of the pooling mechanisms and issue an annual report dealing with his findings.
7. The Committee recommends that at the end of five years, a special summary report, evaluating the success or failure of the residual market mechanism in serving the public, should be prepared by the Superintendent's Office and provided to the Minister to be tabled in the Legislature. In the meantime, if the situation warrants such action, the Superintendent should be obligated to formulate recommendations and submit them to the Legislature.
8. Finally, the Committee recommends that all insurers licenced in Ontario be required by legislation to share in the costs of operating the residual market mechanism. Because of the residual market mechanism is essential to the availability of compulsory insurance, the Committee maintains that participation in its costs be made mandatory.
9. Should implementation of compulsory insurance by the government of the day not include the requirement for a take-all-comers approach to marketing, attention must be given to ensuring that the selected marketing-pooling alternative will serve the interests of the public. In this regard the Committee offers the following observations and recommendations.
 - (a) The Committee expects that the industry will establish a pooling mechanism that is fair in its transfer of risks. Nevertheless, the Committee continues to be concerned about the possibility of unacceptable growth in the size of the residual market.
 - (b) The Committee is concerned about the manner in which an insured is classified as a residual risk and about the "population" of drivers transferred to the Facility.
 - (c) Therefore, the Committee recommends that the industry be required by legislation to inform the insured of the conditions for which he is being transferred to the residual market. The industry should also be obligated to inform the insured when such conditions have lapsed and be prepared at that time to offer him coverage as a regular customer.
 - (d) In addition, the recommendations in points 6, 7 and 8 above should apply whether or not a take-all-comers approach is implemented. The importance of these recommendations would in fact be greater under the alternative methods of marketing compulsory insurance.

Chapter 4—The Motor Vehicle Accident Claims Fund

1. Since there will always continue to be accidents caused by uninsured or unidentified drivers, the Committee recognizes that it is important that the Motor Vehicle Accident Claims Fund or an equivalent mechanism be maintained to pay the claims, as required, of innocent victims.
2. The Committee recommends that, for the present, the Motor Vehicle Accident Claims Act Fund be maintained and, at the same time, that the Motor Vehicle Accident Claims Act be amended to ensure that innocent victims be compensated to the full extent provided for under all forms of compulsory insurance, including Accident Benefits coverage.

PART II: AUTOMOBILE ACCIDENT COMPENSATION

Chapter 5—No-Fault Automobile Accident Compensation

1. This chapter provides a brief statement explaining the present system of compensation in Ontario followed by a brief definition of the no-fault concept.

Chapter 6—Advantages and Disadvantages of the No-Fault Concept

1. In this chapter the Committee briefly discusses a number of the major issues involved in consideration of the no-fault concept, with particular emphasis on compensation for bodily injury. Certain of the Committee's observations and conclusions follow.
2. It has been argued before the Committee that a driver will be willing to pay more in premiums for a small measure of added protection on a no-fault basis, as long as the right to tort action is retained for full recovery from the blameworthy driver. The Committee is concerned, however, that this approach may not ensure that the needs of all persons injured on the roads are adequately provided for, since an affordable no-fault coverage on this basis is likely to provide universal benefits that are too low for the majority of the injured population.
3. In general, the Committee finds that a no-fault system can be structured in such a way as to provide adequate and comprehensive coverage for economic losses. However, the Committee observes that any decision to retain the payment of full damages for non-economic loss would seem to be best accommodated under the tort recovery system.
4. The Committee observes that introduction of no-fault compensation is unlikely to effect a reduction in total automobile insurance costs. However, the Committee concludes that a no-fault programme can be formulated which can compensate the average injured person for substantially the full extent of his economic losses without effecting any significant increase in total automobile insurance costs. This conclusion is, however,

conditional on the significant limitation of payment of damages for non-economic loss.

5. It is the Committee's view that the tort system of compensation which has developed within common law has in fact served the residents in Ontario well, in comparison to less efficient and sometimes abused tort systems in some other jurisdictions.

The Committee has nevertheless been made aware of the opportunity presented by the no-fault alternative for improving upon the present system. In particular, the Committee is convinced that savings will be forthcoming through elimination of the fault investigative process. In addition, it is impressed with the direct accountability of the insurer to his own policyholder established under a first-party settlement process, and it is also impressed with the suitability of a no-fault system to the payment of present and future damages on a periodic or instalment basis.

6. It is argued that the existing fault-based system promotes individual responsibility, while a no-fault system treats innocence and guilt alike and thereby dilutes individual responsibility. The Committee, however, believes that the real deterrents to careless driving fall outside the automobile insurance system and the common law system of liability.

Chapter 7—Own-Vehicle Damage

1. In the Committee's opinion, it is as important to save costs in the vehicle damage area as in the field of bodily injury since overall savings in the automobile insurance industry are an objective.
2. The Committee has been made aware of the following arguments against a no-fault own-vehicle damage system:
 - (a) No-fault insurance means the driver must bear the cost of collision coverage for damage caused by another driver's fault.
 - (b) Many vehicle owners may not want to bear the full cost of collision coverage; they expect to be compensated only in the event that they are not at fault.
 - (c) The success of a no-fault own-vehicle damage system can be endangered by abuse or overutilization.

The Committee observes that solutions have been proposed to reduce the significance of these problems; several of these solutions are mentioned briefly in this chapter.

3. The Committee has been made aware of the following arguments in favour of a no-fault own-vehicle damage system:
 - (a) It is generally argued that improved methods of claims settlement in the vehicle damage area can be achieved by extending the first-party

settlement principle to vehicle damage claims under a no-fault system.

- (b) An important advantage of a no-fault own-vehicle damage plan is said to be the elimination of the subrogation function, resulting in increased accountability of the insurer to his own insured and in elimination of the costs of involving more than one insurer in the settlement process.
- (c) Advocates of no-fault systems contend that appropriate alternatives can be made available under a no-fault own-vehicle damage plan which will tailor coverages and cost to the recovery expectations of the public.
- (d) Finally, it is argued that the integration of own-vehicle coverage with bodily injury coverage in a no-fault system will provide the best means of achieving savings in the automobile insurance system by completely eliminating the investigation of fault.

The Committee will comment on these factors in its conclusions in Chapter 8.

Chapter 8—No-Fault Automobile Accident Compensation: Conclusions and Recommendations

1. In formulating its conclusions, the Committee began by addressing the basic issue: whether fault should continue to be the fundamental factor to be considered in determining whether compensation should be paid for motor accident losses. The Committee is particularly impressed with the capacity of no-fault systems to compensate *all* victims, regardless of fault, rather than paying only the relatively innocent. It is also impressed with the capacity of no-fault systems to reduce adjusting and settlement costs by minimizing fault investigation, so that a significantly larger portion of the premium dollar will be returned to the public in claims payments. The Committee accordingly recommends that "fault" should no longer be the fundamental factor to be considered in determining whether compensation should be paid for motor accident losses.
2. Having reached its conclusion in favour of the general no-fault principle, the Committee then considered the more specific area of compensation for bodily injury. The Committee observed that the advantages of no-fault were even more compelling in this area than in any other. It has therefore concluded that Ontario should establish a full no-fault programme of bodily injury compensation for economic loss and that the new programme should supersede the present Accident Benefits coverage.

3. Turning from questions of general principle to more specific matters, the no-fault bodily injury programme which the Committee recommends for Ontario should include the following detailed characteristics:
- (a) The no-fault bodily injury compensation programme should define all the various economic losses for which compensation is to be paid and the limits (if any) to be imposed on each type of compensation. *All* victims should then be entitled to recover from their insurers (or from the Motor Vehicle Accident Claims Fund, if there is no insurer) to the full extent provided for in the programme. The victim will neither need, nor be able to obtain, recovery from the other driver, or from the other driver's insurer.
 - (b) Compensation for economic losses suffered should include:
 - (i) medical expenses without any monetary limit;
 - (ii) rehabilitation expenses without any monetary limit;
 - (iii) partial or total loss of income should be re-imbursed, subject to a reasonable weekly maximum amount. However, there should be no ceiling in the duration of payments, other than the time required to get back to work;
 - (iv) where there is no *literal* loss of monetary income, but there is nevertheless a loss of services, payment should be made to cover the actual cost incurred. Such compensation should be subject to a reasonable weekly maximum.
 - (v) death benefits should include any reasonable funeral cost and benefits payable to survivors in accordance with a scale of the sort that is now in effect for Accidents Benefits coverage.
 - (vi) if the spouse or dependants have actually suffered a loss of support that exceeds the lump sum benefits provided for in (v), the excess should be paid to them in periodic payments that may be revised or terminated in the event of the recipient's death or re-marriage or the expiration of the period during which the deceased would have provided support to such dependants. Such payments should be made subject to a reasonable weekly maximum amount.
 - (c) The programme to be established should provide for the making of instalment payments in order to provide flexibility.
 - (d) The Committee anticipates that its proposed no-fault programme will reduce disputes over compensation to a minimum,—certainly far below the present level. However, adequate provision should be made for the settlement of such disputes as may arise and so the present arbitration provisions of the standard policy should be retained, together with a full right of resort to the courts.

- (e) Compensation should be extended to provide for the needs of all persons suffering economic losses arising from a motor vehicle accident. In this regard the needs of the spouse and dependent children of the injured driver must be considered. Accordingly, compensation should not be denied to those injured persons who were involved in the commission of a criminal offence such as escaping arrest or who were driving while their ability was impaired through the use of alcohol or drugs. The Committee has concluded that compensation should cover such instances, so that economic losses arising from the motor vehicle system are borne within that system, rather than being borne by other systems such as O.H.I.P.
4. The Committee has been concerned with the arguments that it has heard with regard to the abolition of compensation for non-economic losses such as pain and suffering. Certainly there is a saving to be gained from the elimination of this area of compensation, and this saving is particularly tempting in view of the intangible character of such payments. It is equally significant that the elimination of such damages can end the high cost of fault investigations and adversary proceedings,—savings that are certainly important to the long-term health of any form of an automobile insurance system.

And yet, despite the logic of these arguments, the Committee has concluded that it is wrong to eliminate all compensation for such non-economic losses. The Committee is convinced that these losses represent a legitimate class of loss which should not be disregarded if the objective of generous and realistic compensation for damages resulting from bodily injury is to be met. The Committee believes that there is an expectation among the insured public of compensation for categories of loss such as pain and suffering, and that this expectation should not be denied, particularly in cases of serious injury.

The Committee is convinced that reasonable adjustments can be made in the no-fault programme which will enable some fair compensation for non-economic losses to be paid in appropriate cases without vitiating the basic no-fault concept. The conviction has been strengthened by what the Committee has learned about the operation of such modified systems in Massachusetts, Florida and Michigan. The Committee therefore supports the principle that there should be some provision within the proposed no-fault programme for compensation in bodily injury cases for non-economic losses.

5. The Committee considers that its proposed no-fault programme should include provision for payment of some compensation for non-economic losses by the insurer to the insured in some cases. Such compensation should take the form of a lump sum to be set out on a fixed scale which would provide an exact amount for each type of injury. The Committee

has been interested in particular in the scale that has been established in New Zealand. The amounts should be modest, in keeping with the fact that they are payable to *all* victims regardless of fault and without the need for any evidence of the *actual* extent of the non-economic loss. Furthermore, the scale should allow for payments only where injuries are physically observable and medically certifiable.

6. The Committee recognizes that some cases of bodily injury may be so serious that it would be unfair to limit non-economic compensation to that set out on a scale, in part because scale payments are inevitably only rough approximations and in part because they are necessarily modest in amount. In order to make a fairer provision for the most serious cases, the Committee recommends that a victim who has been injured in a motor accident should be entitled to recover compensation from a third party to the extent of his non-economic losses such as pain and suffering but only in the following circumstances:

- (a) He must be able to establish that he has suffered:
 - (i) serious and permanent injury resulting in substantial and medically demonstrable permanent impairment affecting the resumption of customary activities; or
 - (ii) permanent loss of important bodily functions; or
 - (iii) significant permanent scarring or disfigurement;otherwise he is not to be entitled to make any claim whatever against any third party.
- (b) He must be able to establish at the very beginning of any litigation that the gravity of his injuries fulfils one of the foregoing tests, otherwise he is not to be entitled to continue the prosecution of his claim.
- (c) His right of recovery should be subject to the traditional rules of the law of negligence, so that the customary inhibitions of the fault system will apply.
- (d) The compensation which he may recover should be limited to non-economic losses for which no compensation is provided under the no-fault programme.
- (e) There should be a limit on the amount recoverable under this provision. The Committee considers that \$100,000 is a reasonable maximum.

In order to provide a source from which such compensation can be paid, it will be necessary to retain third-party liability coverage to the extent that such coverage is necessary to pay these "extra-ordinary" claims.

7. Own-vehicle coverage should also, in the Committee's opinion, be included in the overall no-fault programme to be adopted in Ontario. The

Committee recognizes that there is by no means the same compelling importance about ensuring that *all* victims are compensated in own-vehicle damage cases as there is in bodily injury cases. Nevertheless, there are other reasons that are salient. At present, claims for vehicle damage outnumber bodily injury claims by eight to one. The result is that, when vehicle claim settlements are slow or inefficient or denied, a great many motorists who pay premiums year after year are likely to feel that they are not getting their money's worth out of the insurance system. Furthermore, the economies that can be achieved by eliminating fault investigations from bodily injury cases are even greater in vehicle damage cases, because of their greater frequency.

In addition, the accountability of the insurer to the insured is increased under a no-fault system. Under collision coverage, the insurer often pays his policyholder's claim with funds that he then recovers by subrogation from the insurer of the party at fault. That is, he is paying his policyholder with another person's money and consequently may not be concerned about controlling the appraisal process and the costs of repair. As a result, the incentive to contain costs under collision coverage is not as apparent as under no-fault coverage, where the insurer is, in all cases, accountable to his own policyholder for rising costs. The Committee therefore supports the principle of the inclusion of own-vehicle damage coverage within the proposed no-fault programme.

8. The method of inclusion of own-vehicle coverage within the proposed programme must make due allowance for two principal considerations. First, the purchase of own-vehicle coverage should be optional. Second, the Committee considers it essential,—particularly in view of Michigan experience and the Committee's observations in Massachusetts,—that there be a method of recovering deductibles to the extent that a driver is blameless, otherwise the programme will be unfair and thus unacceptable to the public. The Committee therefore recommends that:

- (a) Every automobile policy should contain, as a *mandatory* feature, a new form of coverage under which the insurer will compensate the insured for his first \$250¹ of own-vehicle damage *to the extent that* the insured can establish his innocence in the accident, normally by means of a standardized collision assessment chart. However, no claim will be available against any third party, either by the insured or by his insurer through subrogation.
- (b) Every insured should be able to purchase, if he so chooses, the usual own-vehicle coverage. If the insured has this coverage, his own insurer will compensate him for his own-vehicle damage

1. The Committee in its First Report recommended that the collision deductible be fixed at \$250, without the option of alternative amounts.

above the amount of the deductible regardless of the insured's guilt or innocence in the accident. It bears re-iterating, however, that in no event will any claim be available against any third party, either by the insured or by his insurer through subrogation.

- (c) Every insured should also, at his option, be able to purchase collision coverage in respect of limited recovery situations. If the insured has "limited own-vehicle damage coverage" his insurer will compensate him for his loss over the deductible, but only to the extent that the insured can establish his innocence, normally according to the standards specified on a collision assessment chart or equivalent thereof. If the insured does not buy *any* collision coverage, his own insurer will not compensate him over the deductible amount, nor will he be entitled to seek recovery from any third party.
- 9. The Committee recognizes that the recommendations that it has formulated serve only as an outline for a new no-fault automobile insurance programme for Ontario. It also recognizes that there has not as yet been any opportunity to make any projections as to the cost of the proposed new system, although it is apparent that the savings to be gained from increased efficiency and the reduction in non-economic compensation claims will, in all likelihood, offset any overall increase in other claims costs. Exact dollar projections must inevitably be left to the industry and the Superintendent and a fine tuning of the terms can be conducted on the basis of that information.
- 10. Messrs. Sam Cureatz, M.P.P., Bud Gregory, M.P.P., William Hodgson, M.P.P., David Rotenberg, M.P.P., Alf Stong, M.P.P., and Paul Yakabuski, M.P.P. submit an opinion *dissenting* from the conclusions and recommendations reached by the majority of the Committee in Part II of its Report.

In their dissent, the above members outline their objections to the no-fault programme proposed by the majority of the Committee and include the following observations.

The addition in 1972 of Accident Benefits coverage to the Ontario automobile insurance system was intended to import into the existing system some part of the no-fault concept, without detracting from the basic principle that the function of an automobile insurance system is to provide a means of paying full and fair compensation to those who suffer damage as a result of the conduct of those who are careless.

Experience has shown that it is possible to proceed gradually and consistently with enrichment of the Accident Benefits coverage under controlled conditions so that the increases in costs do not go beyond affor-

dability—and without jeopardizing the power of the system to provide adequate compensation to the innocent.

The objection to no-fault is not so much that it compensates the guilty as that it may compensate them at the expense of the innocent. Accordingly, the wise course to adopt in Ontario is to continue a policy of enrichment of Accident Benefits coverage so that even those who are at fault can be compensated to some degree but only insofar as it is possible to do so without denying full compensation to the innocent and without rendering the insurance system excessively expensive.

The members concurring in this dissent propose that:

- (a) The Province of Ontario reject any no-fault system of motor vehicle accident compensation, such as that recommended in Part II of this Report.
- (b) The Province of Ontario continue its policy of enriching the Accident Benefits coverage on a gradual basis, as experience shows that enrichment is affordable without jeopardizing the primary objective of granting adequate compensation to the innocent victim.
- (c) The automobile insurance industry in Ontario be given the opportunity to make further improvements and savings such as those that have already been effected as a result of the establishment of appraisal centres, the adoption of the collision assessment chart and acceptance of the knock-for-knock principle in Accident Benefits settlements.

PART III: GOVERNMENT PRESENCE IN THE AUTOMOBILE INSURANCE INDUSTRY

Chapter 9—Experience with Government Ownership

1. This chapter provides a general background of the experience with government ownership outside Canada and then deals with the specific experience with government ownership in the Canadian Provinces of Manitoba, Saskatchewan and British Columbia. The Committee reviews in this chapter the history of the government insurers in Canada, their operations and a financial comparison of their operating results with those of the private insurance industry in Ontario. The Committee's interpretation of the material presented in this chapter and its corresponding recommendations are summarized under Chapter 10.

Chapter 10—Conclusions on Government Ownership as an Alternative for Ontario

1. An examination of government automobile insurance jurisdictions throughout the world indicates that government ownership, far from

being an "idea whose time has come" is an idea that has been adopted in only a relatively few western jurisdictions.

2. One of the arguments advanced for the establishment of government insurance systems in Western Canada, was that if all members of the motoring public are compelled to buy insurance, they should not thereby be compelled to contribute to private sector profits. The Committee does not agree that this contention is a justification for the adoption of a government insurance system. However, while the enactment of the compulsory insurance rule does not dictate that auto insurance should be "nationalized", it does necessitate that automobile insurance should be supervised carefully in the public interest.
3. There is a popular misconception that the government automobile insurance corporations in Western Canada provide terms of coverage for the consumer that are unlike those provided in the private sector Provinces. It is quite clear that this is untrue. The terms of the traditional coverages, third-party liability coverage, Accident Benefits coverage and own-vehicle coverage, are substantially the same as those available in Ontario. Indeed, Ontario's minimum liability limit and its recently enriched Accident Benefits are more generous than the protection provided in the western Provinces.

In addition, there is no indication that either system is inherently better suited than the other to the operation of a no-fault automobile insurance programme such as the one which is proposed in Chapter 8 of this Report.

4. Under a government automobile insurance system, all applications for insurance must be accepted, with the result that there is no "residual market" problem.

The Committee has concluded that one of the gravest shortcomings of the private insurance system is the perennial problem of the residual market.

The Committee recognizes that, under a government insurance system, the residual market ceases to be a problem, and the Committee considers this as a major benefit to be derived from such a system. This is especially important when compulsory insurance legislation comes into force because, if a government licenced driver must have insurance in order to drive, government must surely see to it that insurance is available.

Instead of recommending government auto insurance as a solution to the problem of the residual market, the Committee repeats its recommendations that two alternative steps be taken. First, licenced automobile insurers should be compelled to take-all-comers. Second, the industry must be responsible for the establishment of a method of pooling

of its own devising so as to spread the cost of servicing the residual market equitably amongst all insurers and across the entire automobile insurance system. This must be done in such a way that those transferred into the residual market are fairly treated. The Committee expects that the industry will fulfill this responsibility.

5. A one-corporation system is able to provide one common classification system for the entire Province. This is in contrast to the present system in Ontario, whereby different insurers are able to use different classification systems. However, the Committee is satisfied that its recommendations contained in Chapter 15 will provide Ontario with a mandatory standard classification system that will help the consumer to shop intelligently for insurance.
6. The one-corporation system makes it practical to fix rates so as to accomplish perceived social objectives, rather than on the basis of pure actuarial experience. In contrast the private sector holds to the view that premiums should be fixed purely on the basis of actuarial considerations and that any cross-subsidization that is deemed "socially" necessary must be made outside the framework of the insurance system.

While there may be a perceived need for social values to influence premiums, experiences in the government ownership Provinces suggest that a government corporation's unique ability to cross-subsidize can be a source of some dissatisfaction, indicating that such proposals should be approached with caution.

It is impractical to carry out a cross-subsidization programme satisfactorily under a private sector insurance system. On the other hand, the need for such a programme may subside or even disappear under the no-fault system that the Committee has recommended in Chapter 8. One of the important consequences of this plan will be to reduce the importance of fault as an element in the ratemaking process. This will reduce the more extreme contrasts in premium rates between one driver and another, such as the contrast involving the under 25 driver, and it will accomplish this in a manner that is entirely consistent with sound actuarial principles.

7. A government insurance system can draw upon extraneous revenues such as drivers' licence fees and gas taxes, so that it is not limited in its revenues to premiums and investment income.

Two advantages flow from this characteristic of the government corporation. First, through the medium of drivers' licence fees, the cost of the insurance system can be spread so that drivers as well as owners bear some part of the cost. Secondly, by means of a gas tax, there can be some direct relationship between the number of miles that a motorist drives and therefore the extent of his exposure to the risk of accident,

and the amount of his contribution to the insurance system. The Committee recognizes these advantages but it has concluded that they are not of a compelling nature.

The Committee also considers that the use of such extraneous revenues may disguise the real cost of an insurance system. In contrast, the private sector system has the advantage of making consumers more aware of the cost of the automobile insurance system.

8. One stop claims centres can be established by government insurance corporations with the result that there is a significant increase in convenience to the motoring public. This advantage diminishes as private insurance companies evolve co-operative methods of claims settlement such as the I.B.C.-sponsored Appraisal Centres and the use of collision assessment charts to settle disputes. As indicated in Chapter 13, the Committee is convinced that further improvements can be made by the Ontario industry.

The establishment of a no-fault automobile insurance system as recommended by the Committee in Chapter 8 of this Report, would provide the opportunity to move even further to one stop methods of claims settlement.

9. In Ontario, most private company investments are in government securities that are hardly different from the securities in which the government corporations invest. The Committee does not see any distinctive characteristic in government ownership insofar as the investment policies of the government corporations are concerned.
10. The adoption of government automobile insurance facilitates the establishment of a fully effective system of enforcing compulsory insurance by providing for the close integration of the vehicle licencing and automobile insurance systems. As a result, the concept of an irrevocable policy coterminous with a valid licence plate has been successfully implemented. The Committee considers that this is a major feature of the government insurance system, and it considers fully effective enforcement to be fundamental. However the Committee is still convinced that the private sector, despite some protestations, will be able to develop an efficient compliance system, including an irrevocable policy, if necessary, through joint efforts with government. Until such time as the industry proves unable to do so, the Committee sees no compelling advantage to this particular characteristic of government insurance.
11. One-corporation insurance systems are said to be especially well-suited to the operation of worthwhile ancillary activities such as safety research, loss prevention programmes, automobile repair studies and driver education programmes. While this appears to be true, the Committee has observed that the private sector has been very effective in

carrying out jointly sponsored projects, particularly through the auspices of the industry-wide Insurance Bureau of Canada. The Committee has concluded that the demonstrated ability of the companies to work together on such projects leaves no significant advantage to the government corporations.

12. The level of apparent efficiency of the government insurance corporation is higher than that of the Ontario insurance companies. The Committee has taken great care in reviewing the basis for this comparison. It has concluded that, while the financial information provided to it may not be exact in every detail, it is substantially correct and the comparisons which have been made are fair in substance. The Committee cannot quantify this higher efficiency.

Having reached the conclusion, the Committee considers that the apparent relative inefficiency of the industry in Ontario is of serious concern. The Committee believes that improvements can be achieved in the operating cost structure of this industry, certain of which may find their origin in the operating methods of the government insurance system.

13. The Committee has concluded that any higher efficiency afforded by the monopolistic nature of a government insurance system does not, by itself, justify a change to government insurance for Ontario. This is because the difference in efficiency is not the only test by which insurance systems should be judged. In addition to consideration of dollar efficiency there are other factors to be weighed; for instance, there is a weight or value to be given to such advantages of the competitive system as the ability to choose between companies.
14. Part of the difference in efficiency mentioned in conclusion 12 can be traced to the fact that selling costs of private insurers in Ontario are higher than in the three government insurance Provinces. It has been suggested to the Committee that a justification for at least part of this difference is the provision of more individual service to the public by private insurers. Whether or not this is true, the Committee is convinced that the industry should nevertheless be able to take major steps to streamline its marketing process so that these expenses can be reduced.
15. A further explanation for the difference in efficiency described in conclusion 12 is that claims costs for adjusting and settlement are higher in Ontario. The government corporations enjoy the advantage of one stop claim centres, and it is clear that this advantage is a major cause of the difference.

In Ontario there are counter-balancing factors. There has been a steady improvement over recent years in the degree of cooperation that the Insurance Bureau of Canada (I.B.C.) has succeeded in promoting

amongst automobile insurers. This new spirit appears in the establishment of a chain of Appraisal Centres, in the use of driver assessment charts and other cooperative techniques for settling claims. It is reasonable to hope that this evolutionary process will continue and the Committee would expect to see some closing of the gap in the margin of efficiency.

The implementation of the Committee's recommended no-fault programme will also reduce adjusting costs. Most of the cost of investigating and litigating liability claims should be saved. The great bulk of claims will involve only the insurers and their own insureds. Consequently, insurance companies should be able to settle claims with the same efficiency that now exists under the "one-corporation" systems in the West.

16. Underwriting and policy processing costs are apparently higher in Ontario.

It is true that a large government insurance corporation such as I.C.B.C. should be able to take advantage of certain economies of scale that are not available to smaller insurance companies. And yet Ontario's larger automobile insurers, even though smaller than I.C.B.C., should be large enough to enjoy similar economies. Ontario companies should also be able to increase their use of various cost saving joint projects under the aegis of the I.B.C. Whatever methods are adopted, it is clear that the private sector must increase its efficiency in order to survive in a world in which not only insurers compete against each other, but also entire insurance systems compete for favour.

17. The Committee has given due consideration to some of the consequences that might reasonably be expected to flow from the adoption of a government automobile insurance system for Ontario. Automobile insurance constitutes a significant portion of the entire field of general insurance in Ontario. There is a real danger that, if the industry were forced out of the automobile insurance field, the result might well be a significant withdrawal from the general insurance field, with resulting problems of lack of capacity in such other crucial areas as property insurance. It is not possible to forecast the full extent of these consequences.
18. The monopolistic nature of the government corporations, which is said to be the source of much of their strength is also, in the Committee's opinion, the source of their potential weakness. When there is no competitive atmosphere to force operating efficiencies upon management, the eventual result might be inefficiency.

However, to point to this danger in a government monopoly is not to reject the government insurance corporation for all time and under any

circumstances. Rather it is to emphasize that, whatever the present weaknesses of the private sector may seem to be, and whatever the contrasting appearance of strength of the government monopoly, the government monopoly carries within itself a weakness that must inevitably be weighted in the balance.

19. In summary, the Committee has concluded, after weighing the various characteristics of the government automobile insurance systems, that Ontario can be better served under a system of automobile insurance operated within the private sector than by the adoption of a government automobile insurance system.

The Committee has not reached this conclusion, however, without certain reservations, the principal of which are:

- (a) that it is imperative that the industry resolve the chronic problem of the residual market;
- (b) that a generally acceptable and well-publicized classification system must be developed and that public confidence be established in the ratemaking process;
- (c) that the industry cooperate in the development of a fully effective compliance system as part of the implementation of compulsory insurance in the Province;
- (d) that any future increases in selling expenses be curtailed through careful programmes designed to make marketing systems more efficient;
- (e) that any future increases in adjusting expenses be curtailed by continued inter-company cooperation and by the implementation of the Committee's cost saving no-fault programme; and
- (f) that any future increases in administration expenses be contained.

The Committee recommends that the Superintendent of Insurance should follow a policy of giving continuous encouragement to the development of programmes within the industry in Ontario for the purpose of achieving the foregoing goals,—goals that the Committee believes that the industry can achieve. Then after a five year period an appropriate legislative committee should re-assess the progress that has been made and should review the conclusions that have been reached in this Report.

20. Messrs. Bud Germa, M.P.P., James A. Renwick, Q.C., M.P.P. and David Warner, M.P.P. *dissent* from the major conclusion reached by the Committee "that Ontario can be better served under a system of automobile insurance operated within the private sector than by the adoption of a government automobile insurance system".

The dissenting members consider the conclusion of the Committee, when read with the major reservations about the private insurance industry, to be only a counsel of delay and not a definite conclusion about the merits of a government system.

It has been possible for the first time in Ontario for a committee of this Assembly to look objectively and carefully at the experience of the three auto insurance systems in force in Manitoba, Saskatchewan and British Columbia. It would be the expectation of the dissenting members that this Second Report of the Committee, particularly in those areas dealing with private versus public ownership of automobile insurance, will now be studied objectively throughout the Province in anticipation that the people of the Province will recognize the significant advantages in cost and efficiency of a government system.

Chapter 11—A Government Presence in Rate Regulation

1. In recording its conclusion in the preceding chapter that the business of automobile insurance should continue to be conducted in Ontario by the private sector, the Committee also concluded that there is a fundamental need, particularly when a compulsory automobile insurance rule is established, for a governmental presence in the field of automobile insurance supervision and this applies specifically to rate regulation.
2. In Ontario at present, the Superintendent exercises a broad active role in supervising the licencing of companies, in monitoring their marketing and claims settling conduct including their relationships with individual consumers, and also in providing a vigorous regulation that is designed to prevent insolvencies.
3. A broader form of rate regulation is embodied in sections 365 to 367 of The Insurance Act of Ontario. These sections empower the Superintendent to order, after due notice and a hearing, an adjustment of auto insurance rates whenever they are found to be "excessive, inadequate or unfairly discriminatory or otherwise unreasonable". However, these sections have never been proclaimed in force.
4. In the Committee's opinion, more emphasis is required in Ontario on rate regulation in order to achieve a better balance between financial stability and the other objectives of rate regulation.
5. There are three major methods of rate regulation. The first involves a rigid rate regulation system under which a governmental authority fixes maximum rates, exact rates or a range of rates and these govern the charges that may be made for the various categories of risk. An insurer is then prohibited from violating these rigid standards.

Secondly, rate regulation can also take the form of a prior approval sys-

tem wherein insurers must apply for approval of all rate changes before the new rates can be put into effect.

The Committee rejects these types of regulation as a long-term, or permanent approach to rate regulation. The Committee has observed that such systems do not encourage rate reductions, nor do they even ensure that rates are kept to a minimum which is consistent with financial stability, affordability, and universal availability of coverage.

The third major method of rate regulation involves the use of a body of regulations designed to perpetuate fully competitive conditions in the market place. This is termed "open competition rate regulation." This method is based upon the theory that such competition will in itself minimize premiums and ensure the existence of a reliable and efficient insurance system.

6. The Committee has concluded that open competition rate regulation is the form of automobile insurance regulation which is best suited to the present market conditions in the Province of Ontario.

While there would appear to be competition in the Ontario automobile insurance market place at the present time, the Committee has, however, observed that there are no formal set of criteria for recognizing competitive conditions and for monitoring business activity in such a way as to promote a maximum of competition. Accordingly, the Committee has concluded that there is a need to carry out studies that will formulate a complete set of criteria for evaluating competition, and will permit the establishment in the immediate future of a fully detailed system of rate regulation based on promoting open competition.

7. An open competition system of rate regulation must not be considered out of the context of the overall topic of regulation and supervision of insurance companies; especially in relation to solvency and liquidity matters. The Committee therefore proposes to proceed, as it reviews other forms of general insurance, with a more detailed investigation of the entire topic in the course of its consideration of the role and function of the Superintendent's Office. This detailed investigation will include:

(a) An Open Competition System

- The development of a suitable set of criteria for evaluating competition.
- The establishment of the methods and mechanisms, including public reporting requirements, needed for regularly monitoring the existence and extent of competition in the Ontario insurance industry.
- The advisability of legislating these new requirements or providing for them in regulation.

(b) Solvency and Liquidity

- Further consideration of the appropriateness of the solvency and liquidity rules as they pertain to the other-than-life insurance industry.
 - Further consideration of the need to supplement or amend the present solvency and liquidity rules to make them more meaningful to present conditions.
 - The advisability of legislating these rules or new requirements or providing for them in regulation.
8. The Committee will instruct its staff to work closely with the Superintendent of Insurance on these matters. Recommendations will then be submitted in the context of the entire other-than-life insurance industry, rather than within the constraints of this Report on automobile insurance. In order to provide broader safeguards to the public interest in Ontario, the Committee is hopeful that this investigation will achieve the appropriate balance between the surveillance of insurance company solvency and the other objectives of rate regulation.
9. While the Committee rejects rigid rate regulation as a long-term, or permanent approach, it nevertheless recognizes that some readily-available stop-gap method of controlling rates may become necessary in the short-term, pending the formulation of the more sophisticated long-term solution. The Committee therefore recommends that consideration be given to the review and proclamation of sections 365 to 367 of The Insurance Act and the granting to the Superintendent of more effective powers for enforcing compliance with those sections if the need should appear necessary in the interim.

PART IV: MARKETING, ADMINISTRATION AND CLAIMS ADJUSTING COSTS

Chapter 12—The Operating Cost Components of the Ontario Automobile Insurance Industry

1. This chapter identifies the operating costs incurred by the automobile insurance industry in Ontario for the major functional components of acquisition, underwriting and policy processing, and claims adjusting.

Chapter 13—Opportunities for Operating Cost Savings in the Ontario Automobile Insurance Industry

1. The Committee emphasizes the need for continuous improvements in operating efficiency as a means of curtailing the escalation of premiums. It strongly encourages the industry to place emphasis on the search for new technology and on the utilization of the present techno-

logy. The Committee maintains that both the insurance companies and the agency network must strive to improve systems and procedures, to eliminate redundancies, and to improve management processes by utilizing the administrative, training and development and other facilities in their respective trade associations. More specific comments and conclusions in this regard follow.

2. With respect to the estimated total costs of the marketing or acquisition function in the Ontario industry, the Committee observed that commission paid to agents is the most significant element of cost. In its study of government ownership the Committee observed a lower level of selling expenses associated with the substantially reorganized delivery system in the government insurer Provinces. It has been suggested to the Committee that a justification for at least part of this difference is the provision of more individual service to the public by private insurers.
3. It is nevertheless the Committee's recommendation that the industry examine ways of improving the efficiency of marketing the compulsory insurance product. The Committee expects that improved efficiency will permit an eventual lowering of the commission rate on compulsory coverage or at least will prevent substantial future escalations by controlling costs.
4. With respect to the estimated total cost of the underwriting and policy processing function in the Ontario industry, the Committee found it difficult to see how major improvements could be made without major changes to the present classification system and underwriting methods.
5. The Committee recognizes that implementation of compulsory insurance and simplification of the classification and rating system could result in some measure of longer-term savings in the underwriting process.
6. With respect to the estimated total cost of the claims adjusting function in the Ontario industry, the Committee is convinced that substantial potential for improvement appears to exist in this area. This potential can only be realized by providing for one stop centralized appraisal and claims adjusting.
7. The Committee recommends that the insurance industry be encouraged to undertake a feasibility study of the mechanism that would be required to incorporate on-site adjusting in an industry Claims Centre in order to provide one stop appraisal and adjusting.
8. In the meantime, the establishment of further drive-in Appraisal Centres, as already initiated by the Insurance Bureau of Canada, should be undertaken, until methods of incorporating the adjusting function are investigated. A practical method of funding and cost sharing among all

companies, and not just members of I.B.C., should also be investigated.

9. Potential for improvement in the claims adjusting process can also be sought by examining the adversary system. It would appear to the Committee that the most effective way to eliminate the costs inherent in the present adversary system is through introduction of the Committee's proposed no-fault programme as proposed in Part II of this Report.
10. As long as the adversary system continues, the industry should be encouraged to adopt methods of settlement that facilitate improved efficiency in paying third-party claims. In addition, the industry should be encouraged to provide public disclosure of segregated legal and adjusting costs either through the I.B.C. or through the Superintendent's Office.
11. Certain of the costs of the adversary system, such as the claimant's legal expenses, fall outside the control of the insurance industry.

Accordingly, the Committee addresses the following recommendations to the Ethics and Public Relations Committees of the Law Society of Upper Canada and the Advocates Society of Ontario regarding their public interest responsibilities:

- It is imperative that vigilance be maintained to discourage any practices involving the use of contingency fees.
 - Adequate and full disclosure of estimated fees and disbursements should be provided by all legal practitioners prior to acting for the public in claims settlement matters.
 - A liaison between these associations and the Superintendent's Office should be established to develop an appropriate form of monitoring the legal costs of claims settlement from the claimant's point of view. Legal fees and disbursements paid directly by claimants are presently subject to the standards and regulations of the Law Society of Upper Canada and fall outside the present insurance regulatory process. Yet these costs represent a substantial cost inherent in the existing system of claims settlement. The Committee encourages the Law Society of Upper Canada, as a self-regulating professional body, to undertake a study, on behalf of the public it serves, to determine the costs incurred by claimants in the procurement of legal advice regarding the matter of auto insurance claims.
12. The Committee is also concerned about the present practice of expense loading in this Province. It is entirely possible and likely that certain rating categories bear a disproportionate share of expense costs and, to this extent, rates in these classes may be unfair or inequitable.
 13. The Committee encourages the industry in Ontario to undertake a more equitable method of allocating and distributing expenses. The Commit-

tee recommends that the industry begin immediately to investigate procedures whereby costs can be applied in proportion to the level of work involved on a policy. The Committee has commented further on this matter in conclusion 3 of Chapter 16.

14. The Committee further recommends that the industry provide the Superintendent with the results of its investigations and continue to provide relevant expense data compiled under industry reporting systems, such as the I.B.C. "Expense Allocation and Reporting System". This information should be assessed by the Superintendent with the intention that he issue at the end of five years time a report indicating the progress, or lack of progress, of the industry in developing a more equitable expense loading system.

PART V: THE RATING CLASSIFICATION SYSTEM

Chapter 14—The Present Rating Classification System in Ontario

1. During its deliberations leading to the preparation of its First Report, the Committee reviewed in considerable detail the methods used by the insurance industry to set automobile insurance premiums and identified a number of concerns related to:
 - The need for a classification system that is entirely objective and actuarially sound. Certain aspects of the present classification system appear to be arbitrary or subjective.
 - The need for a clear and understandable system of classification, a condition which is not apparent given the large number of classes in the present system.
 - The need for the calculation of premiums to be based on a set of objective, clear and understandable criteria.
2. In this chapter the Committee reviews the present classification system in Ontario with particular emphasis on two matters: the degree of standardization, and the objectivity or statistical base of the various factors used.
3. Many variations from the standard factors reported to the Statistical Division of I.B.C. are apparent in the classifications used by the individual insurance companies in the preparation of their rate manuals. The Committee has been informed that the extent of the deviations from "standard" in the practices followed by individual companies is one of the subjects currently being reviewed jointly by representatives of the Superintendent's Office and the industry. The Committee expresses its concern about these variations in that some companies may be applying rating factors on which there may not be sufficient or accurate loss experience data so that the premium burden borne by certain policyholders may not be fair or equitable.

4. Secondly, the Committee is concerned that the extent of variations in the classification systems in use in the industry creates confusion about the manner in which prices are determined and thereby hampers the ability of the consumer to price-shop. It is the Committee's view that, because the vehicle owner influences the price he pays for insurance coverage, he has a right to understand *how* he influences price. This understanding could likely act as an incentive for better driving and fewer claims and, at the same time, would facilitate and perhaps encourage price-shopping.
5. It is the Committee's strong conviction that the numerous classification systems presently in use do not permit an understanding by the insured of the characteristics used to determine the rating group into which he falls and the price he must pay.

Chapter 15—Standardizing the Rating Classification System

1. The Committee recommends the establishment of a mandatory basic rating classification system, with which all insurers selling automobile insurance in the Province would comply, as a constructive method of ensuring that a vehicle owner can price-shop for his insurance. The features of the Committee's recommended mandatory standard classification system are outlined below.
2. Of necessity, such a classification system would be based initially on the general criteria presently used in the Province for rating purposes. Standardization of this structure would permit ready identification of the "cells" into which an individual insurance buyer would fall. Each company would then be required to establish rates for each cell or segment of the market place to which it is prepared to sell.

The structure making up the classification system should be designed around mandatory definitions of the factors to be taken into account in rating, for example, at present:

- the rating territories,
 - the age of the operator and the use to which the vehicle is put,
 - the accident record of the driver,
 - the limit on third-party liability coverage,
 - the deductibles on own-vehicle coverage, and
 - the value of the insured's vehicle.
3. In order to ensure that the drivers are given an opportunity to understand the manner in which their premiums are determined, the factors taken into account in determining their "cell" for rating purposes should be noted in straightforward language, rather than by codes, on all applications for insurance, insurance policies and insurance renewal notices.

In general, under either the present system or under a standard classification system, the Committee recommends that the industry be required by

legislation to inform all policyholders of the criteria used by the insurer to classify the vehicle owner to a particular rate category. Disclosure of the criteria should be in writing and should form part of the policy application and all related forms.

4. The Committee recommends that all reporting of policy transactions under the Statistical Plan be made on the basis of the mandatory classification system.
5. The Committee recognizes the potential inflexibility of standardized rate classes. The Committee is concerned that the industry's ability to introduce new ideas could be inhibited with standardization. For these reasons the Committee considers that the potential rigidity of a mandatory standard classification system should be modified in the following regard.

To accommodate the orderly introduction of new concepts of insurance in the Province, it is necessary to establish a mechanism for introducing new classification "cells". The Committee recommends that the establishment of new rating groups or coverages should be subject to the prior approval of the Superintendent's Office. Concurrent with this approval, amendments should be made to the Statistical Plan to require the separate reporting of policy transactions for these new groups or coverages so that objective and statistically based experience data could be developed and in time become part of the mandatory basic classification system.

The introduction of such concepts as unlimited liability coverage and no-fault insurance would necessitate the following of approval procedures along the lines of those suggested above and would require the close co-operation of the insurance industry and the Superintendent's Office. The mandatory rate classification system must be flexible enough to allow for new and different concepts of insurance for Ontario. In general, any exception to the use by companies of objectively and statistically justified factors in the classification system should require the prior approval of the Superintendent's Office.

Chapter 16—Discrimination in Rating

1. The factors taken into account in the rating classification system presently in general use in Ontario have developed by evolution from "socially" acceptable classifications of vehicle owners and drivers dating back in many instances half a century. The Committee is concerned, however, that many of the factors currently used in rating vehicle owners and drivers for automobile insurance discriminate against certain groups of the driving public. In this regard the Committee has reviewed the main features of the classification systems in use or proposed in several other jurisdictions.

2. The Committee recognizes the need for an appropriate rating classification system if the second principle of insurance ratemaking is to be satisfied,—that the premiums charged to individuals should vary according to the degree of risk or hazard they impose in the system. However, the Committee is inclined to concur with the conclusions reached in the studies in Massachusetts and Florida that the present classification system is discriminatory and unfair by overcharging those good drivers who might be members of a high risk class for reasons beyond their control, such as their age or sex.
3. The Committee's concern in this regard is compounded when it reviews the industry's traditional methods of expense loading and paying agents' commissions. In general, both expenses and commissions are calculated as percentage add-ons to a basic premium. To the extent that "discrimination in rating" results in penalizing certain classes of drivers, the premiums these drivers must pay are made even more unacceptable by the current expense loading practices.
4. The Committee is impressed with the arguments in favour of eliminating age, sex and marital status as criteria to be used in determining automobile insurance premiums, and it urges the industry and Superintendent to develop alternative criteria. The Committee considers that more appropriate criteria would be driving experience, driving record, and miles travelled if an objective measurement of this latter factor could be found.
5. The Committee is greatly impressed with arguments in favour of a classification system that provides an incentive to individual drivers to drive more carefully and that rewards safe driving with lower insurance premiums. It is the Committee's view that "good-driving incentives" should be made particularly attractive to young drivers. The Committee encourages the industry and the Superintendent to give attention to this matter.

APPENDICES

APPENDIX A

(referred to in the Preface and Introduction)

SELECT COMMITTEE ON COMPANY LAW FIRST REPORT ON AUTOMOBILE INSURANCE

Conclusions and Recommendations

The following is a summary of the conclusions and recommendations that the Committee has reached, as set out in the First Report.

PART I—Preliminary

Chapter 1. The Motor Vehicle System in Ontario

1. In order to appreciate the magnitude of the business of automobile insurance it is necessary to recognize the magnitude of the motor vehicle system which it services.
2. The number of licensed drivers in Ontario has increased to the point where 70 percent of the population over 16 is licensed.
3. The growth in the number of motor vehicles has been even more rapid, so that there is now approximately one automobile per household in Ontario.
4. The Ontario road system now consists of some 97,780 miles of road and the use of these roads has increased because Ontario drivers are using their automobiles more frequently and they are going longer distances.
5. Driver action, rather than driving conditions, is the cause of most accidents. Driver involvement in accidents decreases as age increases, so that a greater percentage of sixteen-year olds are involved in accidents than sixty-five year olds. Accident frequency is highest in Toronto, with 66.4 accidents per thousand population against 27.7 accidents per thousand across the province.
6. There has been a continuous increase over the years in the overall number of accidents and in the losses that have been incurred. There has also been an increase in the accident rate per million miles travelled.
7. Total economic losses from motor accidents are immense,—well in excess of \$450,000,000 in Ontario in 1975.
8. The motor vehicle system constitutes an immense field for the automobile insurance system to service.

Chapter 2. The Role of Automobile Insurance in a Mobile Society

1. Society has developed a variety of responses in an effort to cope with motor accident losses. These include safety engineering for highways,

safety devices for automobiles, driver education programmes and law enforcement campaigns, all of which the Committee applauds.

2. However, so long as there are roads and automobiles there will be economic losses from accidents. As a result, there is no escaping the problem of how society should distribute, or share, motor accident losses. This is the fundamental concern of the Committee.
3. Our law has adopted negligence as the basis for imposing liability in motor accident cases. However, our society seeks to distribute this liability for economic losses from accidents by the automobile insurance system.
4. The automobile insurance system takes the loss which would otherwise fall on the negligent driver and distributes it throughout the insured driving community generally. This is the essence of our society's loss distribution system.
5. The Committee acknowledges and supports the basic principle of automobile insurance but it recognizes that there is a need for a great many practical improvements in the way in which our system of loss distribution actually works and this is the theme of this Report.

PART II—The Standard Automobile Policy

Chapter 3. An Overview of the Standard Automobile Policy

The policy governs the circumstances in which, and the extent to which the insurance system protects the public and distributes losses. The Committee therefore turned its first attention to the terms of the policy.

1. The policy should continue to be in a mandatory standard form, authorized by regulation, as currently provided for in the Insurance Act.
2. The policy should be completely rewritten so as to convert it into as clear, unambiguous and readily readable a document as its nature permits.
3. When the policy has been rewritten in a more acceptable form the Insurance Act should be amended to require the insurer to provide the insured with a copy of the policy rather than merely providing a certificate, as is the present practice. However, it should be necessary to do so only when the policy is first issued and when terms are changed. The mere act of renewing the policy should not necessitate the delivery of a further copy of the policy.
4. The present application provides that the insurer is not to be liable under its third party liability coverage for any loss or damage resulting from bodily injury to or death of any occupant of an automobile (other than

one of the private passenger, station wagon or bus type) if at the time of the accident more than three persons (exclusive of the driver) were occupants of the automobile. The Committee disapproves of this restriction and recommends that it should be deleted in its entirety.

5. The wording of Statutory Condition 4(5) should be amended so as to make it clear that, while the insurer is not liable for any more than the actual cash value of the insured automobile at the time loss or damage occurs, the reference to "actual cash value" is a reference to the *retail* price that would have to be paid to replace the automobile rather than the wholesale price at which the automobile could have been sold immediately prior to the occurrence of the loss or damage. Furthermore, the phrase "with proper deduction for depreciation" as set out in this statutory condition is redundant and should be deleted.
6. Statutory Condition 4(5) should be further amended to provide that the insurer is not to be entitled to call upon the insured to contribute toward the cost of repairs even though the replacement parts are of a greater cost or value than the replaced parts, unless the total effect of repairing the automobile is to increase significantly the actual cash value of the entire vehicle above its actual cash value prior to the accident.
7. The limitation period set out in Statutory Condition 6(3) should be extended from one year to two years.
8. Another limitation period related to motor accidents, which is little known, should also be extended. Section 267 of The Railways Act, R.S.O. 1950, (sic), Chapter 331 should be repealed and replaced with a two year limitation period rather than the current one-year period.

Chapter 4. The Application Form

1. The form of application for automobile insurance should be clarified and simplified and in particular certain items should be shown in the clearest terms:
 - (a) that certain designated questions on the form are being asked for the purpose of classifying the applicant so that his premium can be calculated.
 - (b) that the information required by the foregoing questions constitutes *all* of the information that may be taken into consideration in calculating the applicant's premium. (Recommendations regarding the undesirable practice of using "subjective" information in the underwriting process are dealt with in Part III below).
 - (c) The application should show the precise classification to which the applicant has been assigned for premium calculation purposes, and exactly why he was assigned to that class, and that the premium that he is required to pay is in fact the premium applicable to that class under the insurer's standard rate manual.

- (d) The applicant, if a married woman, should not be required to disclose her husband's occupation or business.
2. The termination date of the policy, as set out in the application form, should be subject to a ten-day grace period.
 3. The application form should be made clearer by setting out in bold-face type in Item 4 that the only coverage provided by the policy is that for which a premium is specified on the face of the application and that there is no other coverage provided by the policy.
 4. The policy should be clarified in order to make it quite clear that "car-pooling" is permissible without the policyholder's rights being impaired in any way.
 5. The application form should distinguish between those questions on it which relate to the absolute unwillingness of the insurer to accept the application and the questions that relate merely to the calculation of the premium amount. Each type of question should be clearly labeled to indicate separately consequences of incorrect answers.
 6. Item 7 requiring particulars of all accidents, losses or claims within three years preceding the application should include the words "if known" so as to protect the policyholder in cases where accidents may have occurred without his knowledge.
 7. Item 10 purports to warn the applicant as to the consequences of misrepresentation or breach of contract and yet the language is obscure. The Committee recommends that this intended warning should be phrased more clearly.
 8. The application form should set out an acknowledgement by the insurer that it is its responsibility to apply the correct rating class to the insured and that it will calculate his premium accordingly and in his best interest.

Chapter 5. Policy Section A:

Third Party Liability Coverage

1. The policy contains a provision exempting the insurer from its obligations under third party liability coverage if an accident occurs while the automobile is used for towing an owned trailer not described in the policy, if the trailer is designed for use for passenger carrying, demonstration, sales, office or dwelling purposes. The insurer should not be exempted from liability under these circumstances and both the policy and the application form should be amended accordingly.
2. Additional Agreement (3). The policy provides that the insurer must pay interest on third party liability claims from the date of entry of judgment. Since the policy may have effect in some jurisdictions where interest is

payable by law from some earlier date, this provision of the policy should be amended. The insurer should be required to pay all interest coming within its third party liability coverage.

Chapter 6. Unlimited Third Party Liability Coverage

1. The Insurance Act should be amended so as to provide that all third party liability coverage be increased from the present minimum limit of \$100,000 to an unlimited amount.

Chapter 7. Policy Section B: Accident Benefits Coverage

1. The Committee has decided not to make any recommendations at this stage in its proceedings as to the desirability of adopting an extended no-fault programme. At this time it proposes improvements in the present accident benefits coverage.
2. Accident benefits coverage provides for payment of benefits to cover all reasonable expenses incurred within four years from the date of the accident for necessary medical, surgical, dental, hospital, professional nursing and ambulance services and, in addition, all such other services as are essential for treatment or rehabilitation. This benefit currently has a maximum limit of \$5,000. This amount should be increased to \$25,000 per person. It should be made clearer that this benefit also covers payments for medical rehabilitation and occupational retraining necessitated by the accident. The Committee notes a substantial need in the province for adequate rehabilitation and retraining programmes and facilities for the assistance of those who are injured in automobile accidents.
3. The amount payable to cover the cost of the funeral of a person killed in an accident should be increased from the present amount of \$500 to \$1,000.
4. Death benefits in the case of persons killed in accidents should be the same for either spouse, irrespective of whether it has been the husband or the wife who has been killed. This benefit should be increased to \$10,000. In other cases the death benefit should be increased from the present amount of \$1,000 to \$2,000 where the deceased was five years of age or over and from the present amount of \$500 to \$1,000 where the deceased was under five years of age.
5. Total disability benefits which are currently \$35 per week maximum in certain circumstances and \$70 per week in other circumstances should be increased to \$70 per week and \$140 per week respectively.
6. The definition of "dependent children" should be broadened to include children of any age who are dependent for support because they are attending a school, college, or university.

7. The accident benefits coverage provides for payment of those expenses described in paragraph 2 above which are, in the opinion of the injured person's *attending physician* and of the insurer's medical advisor, essential for treatment or rehabilitation. Recommendations have been made to the Committee to the effect that the term "attending physician" precludes injured persons from seeking treatment by such practitioners as Christian Science healers, to whom some people turn for help because of religious conviction or other beliefs. The clause should be altered so as to refer to "the opinion of a physician of the injured persons choice" rather than "the opinion of the injured person's attending physician". This will enable a person to take treatment from whomsoever he wishes and will involve him in dealings with a duly licensed physician for the sole and only purpose of obtaining the necessary information for determining his entitlement to benefits.
8. Total disability payments already referred to in paragraph 5 above are provided while the injury "*wholly and continuously*" disables the injured person. These words were added in order to prevent the improper payment of benefits to persons who might be malingerers. However they have worked against honest people who have tried to go back to work only to find that they are unable to stay on the job. The provision should therefore be amended to provide that a person shall not be disentitled to benefits simply because he or she has tried unsuccessfully to resume employment.
9. "An insured person" is defined to include the spouse of a designated insured. This should be broadened so that it recognizes the relationship of "common-law spouses" in a way that is similar to the recognition that has been granted in the currently proposed Family Law Reform Act.

Chapter 8. Policy Section C:

Loss or Damage to the Insured Automobile

1. The provisions of Policy Section C—Loss or Damage to the Insured Automobile should be simplified so as to provide two types of coverage: collision coverage (which includes upset) and comprehensive coverage, which includes any other peril. There is no need for, and there should not be, any further alternative type of coverage under this section of the policy.
2. Loss of Use Benefits where an automobile is stolen should be increased from the current \$8 per day with a maximum of \$240 to \$12 per day with a maximum of \$360.
3. Persons engaged in the business of selling, repairing or servicing automobiles who have collision and/or comprehensive coverage for loss of or damage to an insured automobile are currently required to make necessary repairs at their own *actual* cost. This discriminates against such in-

sured persons because they are thereby precluded from recovering their normal overhead expenses. This provision should be deleted.

Chapter 9. Minimum Collision Deductibility \$250

1. The minimum deductible for collision coverage should be fixed at \$250 and no collision coverage should be available with a lower deductibility feature.
2. Mr. John Ferris, M.P.P., one of the members of the Committee submits an opinion dissenting from this recommendation and recommends that
 - (a) the minimum collision deductible should be \$100;
 - (b) that the standard deductible be deemed to be \$250; and
 - (c) that buyers of the \$100 collision deductible feature should pay premiums that are adequate to cover their share of the excessive adjusting and administrative expenses that they may impose on the automobile insurance system.

Mr. James Renwick, Q.C., M.P.P., and Mr. James R. Breithaupt, Q.C., M.P.P., concur in this dissent.

PART III—PREMIUMS

Chapters 10 to 14. Premiums

The Committee has studied the ratemaking and underwriting processes and has commented on them at length. Because of their complexity, the Committee has instructed its staff and consultants to prepare a detailed report on these and related problems so that the Committee can make more definite recommendations at the end of the second phase of its continuing studies of the automobile insurance system. For the present, however, the Committee has come to the following more or less tentative conclusions:

1. While it is not realistic to expect that existing premium levels can be reduced below their present level, it should nevertheless be possible to stabilize or minimize future increases in premiums.
2. The Committee has grave doubts about certain aspects of the classification system and has accordingly directed that its staff and consultants join with the Superintendent of Insurance and the industry to investigate further and to recommend a classification system that is entirely objective and actuarially sound. The Committee intends to recommend that such a classification system be adopted as mandatory for all automobile insurers in the province.
3. One of the Committee's areas of doubt in relation to the classification system concerns the present system of rating territories and the Committee will expect this topic to be reviewed with special care.
4. The Committee is also particularly concerned about present policies as to the high rates applicable to the under 25 age group. Even if further

investigation indicates that the current high rates applicable to them are actuarially justified, the Committee nevertheless will consider recommending reduction of such rates so that they will not be prohibitive.

5. The principal criterion for a proposed new classification system will be its complete objectivity in contrast with the present underwriting practice of taking various subjective factors into consideration in deciding whether to write a policy. The Committee's intention is to recommend that this practice should be abolished. An applicant should then be judged on the basis only of the authorized criteria and he will be entitled to have his premium calculated accordingly and to be insured upon payment of that premium.
6. The Committee has been concerned about the policy of surcharging because of driver offence records. Its views are as follows:
 - (a) To date, no satisfactory objective proof has been produced to indicate that a direct correlation exists between driver offences and accident proneness and the Committee invites submissions from those who believe that these factors are correlated.
 - (b) Until such a direct relationship is proved, the industry should be prohibited from obtaining driver offence records and from using driver offence information for the purpose of surcharging policyholders.
 - (c) The Committee recommends that immediate studies be instituted on this subject and that any relevant statistics from the Ministry of Transportation and Communications be made available, without identifying the specific individuals to whom such statistics relate.
 - (d) The Committee's concern is that accident proneness is already predictable on the basis of driver accident records and this appears to be actuarially conclusive. By purporting to predict accident proneness on the additional basis of driver *offence* records, it would appear that the industry is placing policyholders in a position of "double jeopardy".
 - (e) If at a later date, sufficient proof is provided to satisfy the Committee that such a correlation exists so as to warrant surcharging, such surcharging should be permitted only on the basis of a scale approved by the Superintendent and also on the basis that the driving records of *all* policyholders be examined and assessed for this purpose.
 - (f) The Committee's principal concern in this context is the present practice of surcharging the ordinary driver who happens to have some modicum of offences, as contrasted with the driver who is such a chronic offender that he is an obvious menace on the road. The problem created by the latter type of driver is dealt with in Chapter 20 which deals with Driver Review Boards.

7. The Committee was initially concerned about the large number of classes in the present classification system and felt that it would be wise to reduce the number of such classes for the sake of simplicity. After further deliberation, however, the Committee has concluded that the provision of an adequate number of properly devised classes within the classification system is essential. In the first place, it ensures that each driver is fairly classified with other drivers posing substantially the same risk to the insurance system. In the second place, the problem of "risk selection" or "creaming" is minimized if there are as many proper classes as is administratively practical. The Committee has therefore tentatively reached a view that an appropriate classification system should have sufficient diversity of classes to accomplish the objectives set out above. At the same time, it is important that the method of classifying a policyholder should be as clear and understandable as circumstances permit.
8. The Committee has been gravely concerned about the inadequacy of the present Facility to provide for the high risk driver and the residual market generally. To date the Committee has not developed a solution to this problem that can practically be imposed upon the industry. However, in view of the Committee's recommendation that third party liability insurance be compulsory, it is essential that the residual market be serviced by the industry. The Committee therefore wishes to state in the most categorical terms that it considers that the resolution of this problem is the responsibility of the industry and that it will expect the industry to submit a practical solution to the problem during the course of the Committee's forthcoming sittings.
9. With respect to accident-free bonuses the Committee is convinced that claims costs would be further reduced if policyholders who are involved in motor accidents were encouraged in cases involving minor damage to pay their own losses as well as the claims made by others to whom they have caused damage. This can be accomplished by a much more effective use of the accident-free bonus system. The workings of this system were very apparent to the Committee during the course of its investigations in the United Kingdom. There, the accident-free bonus was constantly mentioned to Committee members by insured drivers, and a driver's accident-free bonus repeatedly appeared to be a matter of importance and a source of pride to the driver. It is true, of course, that under the rating system prevailing in Ontario, certain advantages accrue to policyholders who continue to be accident-free year after year up to five years.

However, the publicity given by the industry to this advantage appears to be quite inadequate. It is the Committee's conviction that very real savings could be effected in claims costs if far more advertising and publicity were focused on a clearly understandable accident-free bonus

system. Indeed, this topic should be in the very foreground of the industry's advertising program and should be the most visible feature of application or invoice forms. In the first place it should result in a greater degree of care on the part of insured drivers. Secondly, and more significant, it should also result in insured drivers being prepared to settle minor losses themselves rather than reporting them to their insurers and leaving it to the insurers to absorb such losses. Under a realistic, thoroughly publicized accident-free bonus system, it would be obvious to insured drivers that it is more economical to settle minor losses oneself rather than suffer the loss of the accident-free bonus.

Under the present system, the failure to report an accident may be tantamount to a misrepresentation to the insurer and it will therefore be necessary to amend the terms of the application form and to make other corresponding changes in the law so that a driver who settles his own claims in the manner described would not suffer from an increased premium or from the threat of premium increases, policy cancellation or any similar reaction on the part of the insurer.

It has been suggested that the failure to report "self-adjusted" accidents might distort statistical records and driver classification procedures. The Committee is convinced, however, that the advantages that will accrue from the effective adoption of the accident-free bonus system will far outweigh any disadvantages.

More specifically, the Committee recommends the establishment of an accident-free bonus system which will have the following characteristics:

- (a) After five years with an accident-free record, an insured will be entitled to his maximum accident-free bonus and the insurer will state on the face of every renewal certificate in capital letters and red ink the base premium, the total deduction by reason of the accident-free bonus and the net premium payable.
 - (b) In the event of an insured entitled to such maximum benefit having a claim made against his insurer, he will lose one-third of his accident-free bonus in that year.
 - (c) He will be entitled to regain the penalty loss if he has another accident-free year.
 - (d) All policyholders will be encouraged to adjust at their own expense minor property damage accidents and shall not be penalized by their insurers if they fully pay such costs themselves.
10. With respect to investment income, the investment policies followed by general insurance companies are conservative and ultracautious, resulting in minimal investment returns which the Committee views with

concern. This concern is especially strong in view of the fact that much of the funds available for investment consist of premiums paid by the public in advance. As the Committee has repeatedly indicated, the industry's yield from investments has a direct bearing on the premiums that it must charge and the Committee expects the industry to achieve substantially higher yields in the future. The industry should be aware that its hopes of minimal government intervention will best be served by a more effective investment policy.

11. The Committee also wishes to make it clear that it holds tentative views that the funds held by the industry from the public ought to be subject to some degree of direction as to the method in which they are to be invested, particularly so as to accomplish socio-economic objectives that are generally considered important within the community. The Committee believes that this can be done without in any way impinging upon solvency and liquidity rules.
12. With respect to rate regulation, the Committee is not prepared at this stage in its deliberations to recommend governmental rate regulation. However, last year's debate between representatives of the industry and of the Superintendent's office has drawn attention to the matter and the Committee intends to consider the question during the course of the current year.

PART IV—Claims

Chapter 15. Adjusters and Adjusting

1. The Committee disapproves of the use of the term "independent" in relation to adjusters.
2. The insurance company on whose behalf an adjuster operates should be entirely responsible for his conduct, just as it is responsible for the conduct of its full-time, employed staff. The system of licensing adjusters should therefore be abolished.
3. The provisions of the Insurance Act relating to unfair and deceptive acts and practices should be amended to provide that regulations may be made by the Lieutenant-Governor-in-Council, defining unfair acts and practices, including, without limitation, acts and practices related to the process of claim adjustment.
4. The Superintendent of Insurance should then assume the leadership in developing a code of conduct for those in the business of claims adjustment.
5. Claim charts, which are currently used in settling inter-company disputes about collision claims, should be redesignated as "collision assessment charts". These charts must only be used in the course of negotiations be-

tween the companies themselves and never in any way whatsoever in judicial proceedings.

6. The Act should be amended to provide that no insurance company may engage a foreign adjuster to adjust a claim in Ontario without the consent of the Superintendent.
7. The Act should be amended to prohibit corporations from acting as adjusters if they are controlled by non-residents of Canada.
8. Messrs. James E. Bullbrook, Q.C., M.P.P., John Ferris, M.P.P., James Renwick, Q.C., M.P.P., Marvin Shore, F.C.A., M.P.P., Gordon E. Smith, M.P.P., and James R. Breithaupt, Q.C., M.P.P. dissented from recommendations 1 and 2 of this chapter.

Chapter 16. Appraisal Centres

1. The government of Ontario should encourage the development of Drive-in Appraisal Centres such as that which has been established under the aegis of the I.B.C. in Kitchener, so that the entire automobile insurance system will be able to minimize repair costs and adjusting expenses.
2. The Superintendent should ensure that all insurers assume their fair share of the cost of the development of a network of Drive-in Appraisal Centres.
3. The industry should be instructed to give greater publicity to the benefits to policyholders that are inherent in the use of Drive-in Appraisal Centres and to explain that claimants are not charged for the use of the Centres and also that if they wish to go elsewhere for an appraisal, they are free to do so at their own cost.

Chapter 17. Reducing Repair Costs—Automated Appraisal Systems

1. All necessary encouragement ought to be given to the adoption of an *automated* appraisal system as a supplement to the use of Drive-in Centres as recommended in Chapter 16 above. The Committee found the use of the Audatex automated system in Europe to be impressive.

Chapter 18. Reducing Repair Costs—The Thatcham Experience

1. The Committee recommends that a research centre similar to the Motor Insurance Repair Research Centre at Thatcham, England, should be developed and funded through the medium of the Insurance Bureau of Canada with the encouragement of the Superintendent of Insurance and with the co-operation of the automobile industry.
2. The proposed research centre should focus its attention upon the improvement of repair procedures, the development of more efficient repair equipment, the development and encouragement of the marketing of less

expensive crash parts, the training of repair personnel and safety research.

Chapter 19. Medical Costs and O.H.I.P. Subrogation

1. A fundamental change should be made in the entire system whereby the Ontario Hospital Insurance Plan is reimbursed by the automobile insurance industry, because it is cumbersome and costly.
2. The "Statistical Plan" by which automobile accident statistics are compiled should be amended so that the amount of medical and hospital expense resulting from motor accidents can be ascertained. The total of such expenses should then be reported to the Superintendent of Insurance, who should also have the power to verify such amount if he considers it necessary to do so.
3. The Superintendent, having satisfied himself as to the total amount of such expense in any given year, should allocate that amount among all automobile insurers carrying on business in Ontario in the proportion that their share of automobile premium business done in Ontario in that year bears to the total of all such business.
4. Each such insurer should then be required to remit its allocated share of such expense to the Treasurer of Ontario to the credit of OHIP, promptly after receiving its assessment.
5. Upon the implementation of this program the present Subrogation Section should be disbanded.

Chapter 20. Reducing Losses:

Driver Review Boards

1. A Driver Review Board system should be established.
2. Cases should be referable to the Boards by the Registrar of Motor Vehicles, the courts, the police and the public.
3. Tests should be established to determine the circumstances under which a "bad" driver's license should be revoked.
4. The sole object of the Boards should be the protection of the community and not punishment, which should be left to the courts.
5. A Driver Review Board system will be of such complexity that the details of its organization and the criteria for its decisions must be spelled out as the result of a detailed further study which might be done by such persons as the Honourable J. C. McRuer or the Honourable G. A. Gale.

Chapter 21. Compensating the "Guest Passenger"

1. The present legislation that puts a "guest passenger" at a disadvantage in making a claim against his driver should be abolished. The guest pas-

senger should not be required to establish "gross" negligence in order to be entitled to damages from his driver.

Chapter 22. Naming Insurers as Defendants

1. The law and practice of the courts of Ontario should be changed so as to provide that a plaintiff in any action for damages arising out of a motor accident shall institute his action not only against the other drivers and owners involved in the accident, but against their insurers as well. In uninsured driver cases the Motor Vehicle Accident Claims Fund should be named as a defendant in the same way as an insurer would normally be named.

Chapter 23. Inevitable Accident

1. The Committee has considered a proposal that the doctrine of "inevitable accident" be abolished. The Committee has rejected this proposal.
2. Messrs. Vernon Singer, Q.C., M.P.P., Bud Germa, M.P.P., Patrick Lawlor, Q.C., M.P.P. and Floyd Laughren, M.P.P. dissented from this conclusion.

PART V—Compulsory Third Party Liability Insurance

Chapter 24. The Principle of Compulsory Third Party Liability Insurance

1. The Committee recommends that every person who owns a licensed automobile be required to have a valid policy of automobile insurance providing third party liability coverage and accident benefits coverage.
2. Organizations and persons who have heretofore been "self-insurers" or who have not participated in the automobile insurance system as a result of religious opposition to placing faith in an insurance system, should nevertheless obtain insurance coverage so that the public is protected. The Committee believes that they will be able to make their own private arrangements with their insurers which will not compromise their principles.

Chapter 25. Enforcing Compulsory Insurance: The Irrevocable Policy

1. In order to ensure compliance with the compulsory insurance rule, the Committee has considered the advisability of recommending the adoption of a form of irrevocable automobile insurance policy. The Committee is of the view that such a policy may be the most effective method of enforcing compulsory automobile insurance and has referred the matter to its staff and consultants and will make further recommendations in its next report.

*Chapter 26. Compensating the Victim of the Uninsured Driver:
The Motor Vehicle Accident Claims Fund*

1. The Committee is satisfied that the Motor Vehicle Accident Claims Fund must be retained.
2. The Committee recommends that the Fund employ full-time lawyers on its staff to act on behalf of the Fund and that outside lawyers be retained in only the most difficult cases.
3. The Motor Vehicle Accident Claims Act should be amended so as to authorize the settlement of claims involving infants who are only slightly injured, upon the receipt of an indemnifying release from the parents and without incurring the substantial costs of judicial proceedings to approve such minor settlements. This is in accordance with the practice generally followed in minor cases throughout the insurance industry.

PART VI—The Automobile Insurance Industry in Ontario To-day

Chapter 27. The Insurance Companies

1. The Committee recommends that more detailed data be reported to the Superintendent with regard to the automobile insurance business done in Ontario as distinct from other lines of casualty and property insurance. This should be sufficient to ascertain whether policyholders in Ontario are subsidizing or are being subsidized by automobile insurance policyholders in other provinces and whether automobile insurance is subsidizing or is being subsidized by other lines of property and casualty insurance. This should be accomplished primarily by the filing of detailed information on a line-by-line basis and on a province-by-province basis.
2. The Committee has been able to learn at first hand about the abilities of the Superintendent of Insurance and his senior representatives and has concluded that the Province of Ontario is well served in having an extremely competent Superintendent and staff. It would like to express its full confidence in them. It is very fortunate that the province has, in the person of Mr. Murray A. Thompson, Q.C., a Superintendent who has dedicated his entire career to the regulation and supervision of the insurance system and other financial institutions.
3. The Committee nevertheless is concerned as a result of its review of solvency and liquidity tests to find that the authority for these tests is based primarily on the force of long-established custom and practice that has built up over many years in the Office of the Superintendent. These rules which find their sanction in traditional custom have come to be referred to as "in-house" rules. There is generally little or no sanction by way of legislation or regulation to support them. The Committee recommends that any necessary review and study of existing rules as to solvency and

liquidity be carried out immediately by the Superintendent's Office with the Committee's staff and that they report back to the Committee during the current year on the results of such studies. The Committee will then recommend the enactment of such enabling legislation as may be necessary so that regulations can be passed to give such rules as are settled upon the proper force of law. The Committee wishes to add that its tentative view is that the present rules appear to be unnecessarily conservative.

4. The Committee is also concerned that the present Act puts the Superintendent in the position of being, in a sense, legislator, investigator, prosecutor and judge in certain circumstances. A specific example of this occurs in Part XVIII of the Act where the Superintendent, by the making of "in-house" rules is able to some extent to determine what constitutes unfair and deceptive acts and practices in the business of insurance. His Office is then authorized to investigate persons engaged in the business of insurance to determine whether they are involved in such a practice. The Superintendent is then empowered to hold hearings, to make decisions and to issue stop orders.

The Committee recommends that the Superintendent no longer be put in the position where he or his officials appear to be legislator, investigator, prosecutor and judge in relation to their supervisory and regulatory function. To effect this the following steps should be taken:

- (a) The Committee has already recommended that all rules applied by the Superintendent in relation to solvency, liquidity, standards of conduct, etc., be enacted in legislation or promulgated in regulations.
 - (b) The Committee further recommends that any order made by the Superintendent should be subject to appeal. Such appeals should be to the Commercial Registration Appeals Tribunal on questions of fact and to a judge of the Supreme Court on questions of law.
 - (c) The Committee further recommends that the Superintendent be given the power to issue stop orders in cases of emergency, which orders shall continue in force until the final hearing has taken place.
5. The Committee has found that the practice in the preparation of financial statements by insurance companies is to follow a system of accounting principles that is based on the requirements of the government regulations that are applicable to the companies, where those regulations are inconsistent with generally accepted accounting principles followed generally in other fields of business and industry. The Committee has concluded that the result of this practice is that the financial statements of the companies may be confusing to persons who are studying them, particularly to those who are not specialized in insurance matters. The Committee therefore recommends that property and casualty companies, in-

cluding particularly those who deal in automobile insurance be required to publish their financial statements on the basis of generally accepted accounting principles. Where it is necessary because of the requirements of the regulatory agencies to publish additional statements based on regulatory principles, it should be sufficient for the companies to publish reconciliations showing reasons for the differences between the two types of statements.

6. The Committee has noted that federal legislation appears to favour the branches of foreign companies operating in Canada in that:
 - (a) While companies incorporated in Canada must maintain assets equivalent to 115 percent of their liabilities, branches of foreign companies are required to keep on deposit with the Receiver-General and/or a Canadian trustee sufficient investments equal only to 100 percent of their liabilities in Canada, and
 - (b) Branches of foreign companies are not required to present complete financial statements or to have an audit certification as part of their reporting package, although these requirements apply to companies incorporated in Canada. The Committee requests that the Office of the Superintendent, in cooperation with the Committee's consultants, confer with the federal authorities and report back to the Committee as to whether the Committee should request a change in federal requirements so that branches of foreign companies will be treated in the same way that Ontario companies and other Canadian companies are treated.
7. The Committee recommends that members of the industry be directed not to report to the public their underwriting profits or losses as distinct from their total profits on equity, unless a clear warning is included to the effect that the consideration of underwriting results in isolation from the entire profit-on-equity results is misleading.

Chapter 28. The Automobile Insurance Distribution System: Agents, Brokers and Sales Personnel

1. The examination standards applicable to the granting of licences to agents, brokers, and salesmen should be raised in order to ensure that all entrants into this field are better qualified.
2. The Committee has examined the educational programmes being conducted by the Independent Insurance Agents and Brokers of Ontario and recommends that the Office of the Superintendent encourage these programmes and work for their continued improvement.
3. The Committee has considered a proposal for the establishment of a self-regulating council for insurance agents and does not agree with it.
4. The Committee recommends the abolition of the term "independent" or any word of similar connotation by agents so as to avoid any implication

that those who are currently designated as "independent" agents are representatives of the consumer when they are in reality representatives of the insurance companies.

5. The Committee recommends that the Insurance Act be amended so as to authorize the passing of regulations on the recommendation of the Superintendent of Insurance, establishing a detailed list of specific practices or forms of conduct which would be deemed "unfair or deceptive practices" in connection with the sales process.
6. Messrs. Larry Grossman, M.P.P., and James Renwick, Q.C., M.P.P., have presented a dissenting opinion in connection with this chapter, and have also suggested that all agents be permitted to write insurance for all companies doing business in Ontario.

APPENDIX B

(referred to in the Preface)

LIST OF WITNESSES

The following witnesses have appeared before the Committee during the course of its investigations of automobile insurance. The Committee is most grateful to them and, as indicated in the Preface, wishes to express its indebtedness.

Sittings in Toronto

Insurance Bureau of Canada

Mr. Daniel Damov, President

Mr. R. E. Bethell, Director, and President of the Canadian General Group

Mr. F. Clifford, Fraser, Deputy Regional Vice-President, State Farm Insurance Companies, representing I.B.C.

Mr. Edward H. S. Piper, Q.C., General Counsel

Mr. Harry Saunders, Zurich Insurance Companies, representing I.B.C.

Mr. D. L. Wagner, Chairman and Automobile Manager for Canada, Zurich Insurance Company

Insurers' Advisory Organization of Canada

Mr. Edward F. Belton, President

Mr. Herbert J. Phillips, Chief Actuary

The Independent Insurance Agents and Brokers of Ontario

Mr. Sanford E. Phillips, Past President

Canadian Independent Adjusters Conference, Central Region

Mr. Ian Pepper, President

Mr. Roy Holloway, Chairman, No-Fault Committee

Mr. Peter Uffelman, an independent adjuster

The Facility Association

Mr. Colin Atkinson, Deputy Chairman, J.U.A. Committee

Mr. John Matthews, General Manager

Mr. Ronald Walker, Member Research Committee and Director of Industrial Relations, Allstate Insurance Company of Canada

The Advocates' Society

Mr. T. H. Rachlin, Q.C., Chairman, Insurance Committee and Partner of Rachlin, Wolfson & Malach, Barristers

The Consumer Association of Canada

Mrs. Barbara J. Shand, President

Mrs. Helen Anderson, Co-Chairman, National Economics Committee

Allstate Insurance Company of Canada

Mr. Gerald J. Fournier, President

Mr. David S. Murphy, Vice-President, Underwriting

Co-operators Insurance Association of Guelph

Mr. Teunis Haalboom, General Manager and Chief Executive Officer

Economical Mutual Insurance Company

Mr. J. A. Vila, President

Mr. J. H. Argue, Vice-President and Secretary

Royal Insurance Company of Canada

Mr. Alan A. Horsford, President and Chief Executive Officer

Mr. Warren Crawford, Vice-President Personal Insurance Division

Mr. Vern Lamberton, Vice-President, Ontario Operations

Mr. Roger Radford, Vice-President

Mr. John Robitaille, Senior Vice-President

State Farm Automobile Insurance Company

Mr. J. R. A. MacKenzie, Chief Agent for Canada

Mr. Clifford Fraser, Deputy Regional Director

Witnesses from Outside the Province

Mr. Howard A. Baizaire, Administrative Assistant, Automobile Club of Michigan Insurance Group

Mr. Jean Gregoire, Chairman, Insurance Brokers Association of Quebec

Mr. Peter Ingham, Assistant General Counsel, State Farm Insurance Companies, Chicago

Mr. Michael Miller, Actuary, State Farm Insurance Companies, Chicago

Mr. Jack Siebold, General Counsel and Director of Governmental Affairs, Independent Insurance Agents of Michigan

Others

Mr. Peter Alley, Assistant Professor of Business Administration, Faculty of Administrative Studies, York University

Mr. Jan G. M. Beerens, Executive Secretary of the Dump Truck Owners Division, Ontario Trucking Association

Mr. J. B. M. Murray, Consultant, J.B.M. Murray Limited

Sittings in Regina, Saskatchewan

The Saskatchewan Government Insurance Office

Mr. John Green, Q.C., General Manager
Mr. Lee Billesberger, Counsel
Mr. Donald Cody, Executive Officer in charge of Claims
Mr. Mervin Eisler, Manager of the Saskatchewan Division of Motor Vehicles
Mr. David Hick, Executive Assistant to the General Manager
Mr. Ronald Meier, Underwriting Manager, Automobile Section
Mr. Lindsay Neilson, Controller
Mr. Roger Nupdal, Executive Officer in charge of Promotion, Advertising, Corporate Relations and Safety
Mr. Gordon Pritchard, Assistant Director of Claims
And Others

Co-operators Insurance Group

Mr. Frederick Avery
Mr. Kenneth Burgland
Mr. Desmond Haughay

Sittings in Vancouver, British Columbia

Insurance Corporation of British Columbia

The Honourable Dr. Patrick L. McGeer, Minister of Education, and President and Chairman of the Board of I.C.B.C.
The late Mr. Norman Bortnick, Executive Vice-President and General Manager
Mr. Ronald Blackburn, Vice-President and Manager, General Insurance
Mr. Rod Dawson, Rating Manager
Mr. Ralph L. Gillen, Vice-Chairman of the Board
Mr. Thomas Holmes, Vice-President and Manager, Automobile Claims
Mr. Hutchinson, Director of Employee Relations
Mr. Michael McCarthy, Underwriting Manager
Mr. McFarland, Senior Counsel
Mr. B. Penhall, Director of Public Information
And Others

Insurance Bureau of Canada

Mr. Kenneth Malthouse, Manager, British Columbia Division

The Independent Insurance Agents and Brokers of British Columbia

Mr. John Parkinson, Past President

Sittings in San Francisco, California

Rate Regulation Division of the Insurance Commissioner's Office

Mr. Bernard Farrell, Assistant Insurance Commissioner

Mr. Lynn O. Borchert, Senior Rate Analyst

Mr. Mark Gerlach, Rate Analyst

Mr. Kenneth Melie, Rate Analyst

Bureau of Motor Vehicles of California

Mr. Elmer Brown, Chief of the Division of Drivers Licenses of the State of California

Mr. Richard Lehmon, Attorney-at-Law of the Financial Responsibility Section

Mr. Clifford Sheeley, Operations Manager

State Farm Insurance Companies

Mr. Peter Ingham, Assistant General Manager

Mr. Michael Miller, Actuary

Firemen's Fund Insurance Company

Mr. Bud Benedikson, Counsel, Government-Industry Relations Department

Others

Mr. E. Robert Wallach, President of the Plaintiff's Bar of California and Partner of Wallach and Baum, Attorneys at Law

Sittings in Boston, Massachusetts

Commonwealth of Massachusetts, Joint Committee on Insurance

Mr. Edward J. Brennon Jr., Counsel

Senator David J. Foley, Joint Chairman

Office of the Commissioner of Insurance

Mr. Andrew F. Giffen, First Deputy Commissioner of Insurance

Massachusetts Auto Rating and Accident Prevention Bureau

Mr. Lemuel Devers, Chairman

Massachusetts Fair Share Inc.

Mr. James Katz, Research Director

Sittings in Washington, D.C.

Senate Joint Committee on Banking, Housing and Urban Affairs

Mr. G. Buckley, Staff Director

Senate Committee on Commerce, Science and Transportation

Miss S. B. Adams, Research Director

Mr. Michael Mullin, Research Director

Department of Justice

Mr. G. S. Maseritz, Chief of the Legislative Unit, Anti-Trust Division

Sittings in Miami, Florida

The Office of the Commissioner of Insurance

Mr. P. E. Cowie, Assistant Director, Division of Insurance Company Regulation

Mr. C. E. Gray, Assistant Bureau Chief, Bureau of Fire and Casualty, Rate and Policy Analysis

Mr. R. McKenna, Director of the Division of Fraudulent Claims

Mr. A. E. Rummel, Executive Assistant to the Commissioner of Insurance for the State of Florida

Joint Underwriting Association of Florida

Mr. W. Midkiff, Chairman

Mr. H. Schaeffer, Immediate Past Chairman

Florida Agents' Association

Mr. Thomas Pennacamp, President-Elect

General Insurance Company of Florida

Mr. Joseph DiBella, President

Mr. William F. Kissane, Superintendent of Claims

Others

Dr. James Nicholas, Economist, Chairman of the Joint Centre for Environmental and Urban Problems

Mr. Robert D. Shaw, Jr., Insurance Reporter of the Miami Herald

APPENDIX C

(referred to in the Preface)

LIST OF EXHIBITS

The following are the exhibits, submissions, briefs and other documents received by the Committee.

1. Legislature of Ontario,
Terms of Reference
2. The Select Committee on Company Law,
First Report on Automobile Insurance, March 1977, Vernon M. Singer, Q.C., M.P.P., Chairman
3. Ontario Gazette,
List of Insurers Licenced to Transport Business under The Insurance Act, July 30, 1977
4. M. A. Thompson, Q.C., Superintendent of Insurance,
Memo: "Preliminary Background on Insurance Regulations in Ontario"
5. J. B. M. Murray, Consultant,
"The Problems with Automobile Insurance Claims"
6. Facility Association,
Plan of Operation and Articles of Association—June 28, 1977
7. M. B. Dawson, Office of the Superintendent of Insurance,
Memo: "Enforcement of Compulsory Insurance"
8. Woods, Gordon & Co.,
"Summary Review of 'No-Fault' Insurance"
9. J. B. M. Murray, Consultant,
"No-Fault Insurance Plan"
10. Insurance Bureau of Canada,
"Report of the Special Committee—Auto Insurance Plans", July 18, 1974
11. Woods, Gordon & Co.,
Chart: Automobile Insurance Plans—Existing and Proposed
12. Insurance Bureau of Canada,
Draft Legislation to Implement Vari-Plan—March, 1974
13. Lear P. Wood, Office of the Superintendent of Insurance,
Memo: "Vari-Plan Cost Comparison"
14. Insurance Bureau of Canada,
Vehicle Accident Recovery Insurance Plan, October, 1974

15. Ontario Law Reform Commission,
Report on Section 183 of the Insurance Act, 1968
16. Canadian Bar Association,
"What do you lose with Tort Restrictive No-Fault Insurance",
August, 1975
17. Dr. C. H. Brainard,
"I.B.C.'s proposed 'Variplan'—A Cost-Benefit Analysis"
18. Dr. C. H. Brainard,
"A review of the response of I.B.C. on the subject of its Variplan Proposal"
19. Alberta Automobile Insurance Board,
Report on the I.B.C. 'Variplan' Proposal, May 4, 1976
20. Newspaper Articles,
"Perspectives on No-Fault Insurance"
21. Advocates' Society,
Submissions with respect to No-Fault Automobile Insurance
22. Advocates' Society,
Symposium on No-Fault Automobile Insurance, February 8, 1974
23. T. H. Rachlin, Q.C.,
"The I.B.C. 'Variplan'—For or Against the Public?"
24. Ontario Law Reform Commission,
Report on Motor Vehicle Accident Compensation, 1973
25. Dr. Allen M. Linden, Q.C.,
"A Critique of the Ontario Law Reform Commission Report on Motor Vehicle Accident Compensation", 1974
26. Daniel Damov, President of Insurance Bureau of Canada,
I.B.C. Comments on Variplan
27. Thomas C. Jones, Commissioner of Insurance, State of Michigan,
"The Michigan Study—1976"
28. State of Michigan,
Michigan No-Fault Law, Chapter 31, October 1, 1973
29. Howard A. Baizaire,
"Michigan No-Fault Automobile Insurance"
- 30A George Ness, Q.C.,
Charts on Accident Losses and Issues in Compensation
- 30B Woods, Gordon & Co.,
Chart: Automobile Insurance Plans with No-Fault Accident Benefit Provisions; Basic Benefits for Bodily Injury, August, 1977

31. Auto Club of Michigan,
Advertisements on Michigan No-Fault Insurance Bill
32. Independent Insurance Agents and Brokers of Ontario,
"Reaction to First Report on Automobile Insurance by the Select
Committee on Company Law", August, 1977
33. J. A. Vila, President, Economical Mutual Insurance Company,
"Some Comments on No-Fault Automobile Insurance"
34. Murray Thompson, Q.C.,
Memo: "The Typical No-Fault Economic Loss Base"
35. Howard A. Baizaire,
"The Socio-Economic Impact of No-Fault in Michigan"
36. E. F. Belton, President, Insurers' Advisory Organization of Canada,
"Views on Rate Regulation"; and I.A.O. Structure
37. Allstate Insurance of Canada,
No-Fault slide presentation notes
38. U.S. Department of Justice,
The Pricing and Marketing of Insurance, January 1977
39. Lear P. Wood, Office of Superintendent of Insurance,
"A Review of the Government's Current Presence in the Setting of
Automobile Rates in Ontario"—June 1975
40. Allstate Insurance of Canada,
"No-Fault: What's it all about?"
41. Barbara J. Shand, and Helen Anderson,
Consumer's Association of Canada: "Comments on Auto Insurance
and Variplan"
42. Insurance Bureau of Canada,
Survey results: "The Attitude of the Canadian Public towards Auto-
mobile Insurance"—October 1970
43. *The Economist*,
"After the Crash: A Survey of American Insurance", August 20,
1977
44. Insurance Bureau of Canada,
Comparative figures of claims payments made for vehicle repairs in
Canada and the U.S.A.—1975
45. Teunis Haalboom,
The Co-operators: Statement to the Committee
46. Independent Insurance Agents and Brokers of Ontario,
No-Fault Insurance: Statement to the Committee

47. Colin Atkinson,
The Facility Association: Statement to the Committee
48. Royal Insurance Company,
Folder of Articles, Reports and Statements
49. Canadian Independent Adjuster's Conference,
Mr. Roy Holloway: Statement to the Committee
50. Herbert Phillips, Insurance Advisory Organization of Canada,
"Massachusetts Automobile Insurance: 25 years experience"
51. Donald Stuart, Canada Packers Ltd.,
Comments on Unlimited Liability; Parking Lot Accidents; Knock-for-Knock
52. Robert D. Shaw, Jr.,
Miami Herald, Articles on Auto Insurance, "The Great South Florida Ripoff"
- 53A A.Y.D. Koskoff,
"The Nature of Pain and Suffering", *Trial Magazine*, July 1977
- 53B H. Berg and P. Kilby,
"Motor Vehicle Accident Compensation in Ontario: Proposed changes—Are they necessary?", *Western Ontario Law Review*
54. Saskatchewan Government Insurance Office (S.G.I.O.),
Saskatchewan Auto Insurance Guide, 1977, and Information Kit
55. D. C. Hick of S.G.I.O.,
"The Saskatchewan Automobile Accident Insurance Act Explained"
56. Ronald Meier of S.G.I.O.,
"Underwriting for the AAIA"
57. Government of Saskatchewan,
The Reparations Committee, 1976
58. Insurance Corporation of British Columbia,
Fourth Annual Report and Information Kit
- 59A Province of British Columbia,
Motor Vehicle Act
- 59B Province of British Columbia,
Automobile Insurance Act and Auto Insurance Amendment Act; Regulations made under the Auto Insurance Act
- 60A Insurance Corporation of British Columbia,
"All about the B.C. Autoplan"; Owner's Certificate of Insurance; Rating Territories

- 60B Insurance Corporation of British Columbia,
Premium Comparisons
61. Office of the California Insurance Commissioner,
109th Annual Report, 1976
62. Mark Kai-Kee,
“The Rating Examinations Programs under California Law”
63. Mark Kai-Kee,
“Twenty Years Experience under the California Rating Law”
64. State of Oregon,
Bill 967, Legislative Assembly/Senate
65. Hon. Bob Eckhardt, (Texas),
Congressional Record, June 23, 1977, p. E4031, etc., “No-Fault
Automobile Insurance”
66. State of Massachusetts,
Fact Sheet on Merit Rating; No-Fault Property Damage; Staggered
Policies; Competition; Re-insurance and Theft
67. State of Massachusetts,
1976, Chapter 266, *An Act Relative to Motor Vehicle Insurance*
68. State of Massachusetts,
1977, Chapter 365, *An Act Relative to the Rates Charged for Motor
Vehicle Insurance*
69. *Boston Herald-American*,
“Auto Rates Clear Panel, Take Effect”, January 10, 1978
70. Massachusetts, Fair Share Inc.,
“How Fair Share Works”
71. Massachusetts, Fair Share Inc.,
“Highway Robbery”: Fair Share research report documents the fail-
ure of the auto insurance industry to compete in Massachusetts
72. Massachusetts, Fair Share Inc.,
“Stop Highway Robbery”: The Fair Share Plan for Lower Autom-
obile Insurance Rates, September 1977
73. State of Massachusetts, Division of Insurance,
Information about Merit Rating
74. State of Massachusetts,
*An Act providing for Compulsory Personal Injury Protection for all
Registered Motor Vehicles*, 1970, Chapter 670
75. United States Senate,
Hearings on Bill S-1381 “No-Fault”: July 13-20, 1977

76. United States Senate,
Bill S-1710, "Federal Insurance Act of 1977"
77. Congressional Record Senate,
"Senator Brooke introduces Bill S-1710", June 16, 1977, Vol. 123,
No. 104
78. U.S. Department of Transportation,
State No-Fault Automobile Insurance Experience 1971-1977, June
1977
79. Grand Jury of Dade County,
Final Report on Automobile Insurance Rates, January 5, 1978
80. George Bryant,
"Florida Law Can Snag Car Renters", *Toronto Star*, December 3,
1977
81. *Miami Herald*,
"Insurance Panel Offers Little New", "Discriminatory Rate Struc-
tures Under Attack", January 17, 1978
82. *Miami Herald*,
Editorial: Why Ad Hoc Insurance Try Added Up to a Big Nothing,
January 18, 1978
83. *Miami Herald*,
"Congress Urged to Outlaw Bias in Auto Insurance", "Witnesses
Cite Bias Against Young, Widows, GI's", January 18, 1978
84. Florida Insurance Commissioner,
"Report of the Division of Fraudulent Claims", 1977
85. Florida Insurance Commissioner,
Fraudulent Claims Report 78-1, "Florida Stolen Property Index"
86. State of Florida,
Fair Amendment
87. State of Florida,
Insurance Fraud Act
88. Joint Underwriting Association of Florida,
JUA Rate Book and Financial Statements
89. Quebec National Assembly,
Bill 67, *Automobile Insurance Act*, December 1977
90. Murray Thompson, Q.C., Superintendent of Insurance,
Proposal for Amendments to *Part XIV* of the Insurance Act, "Agents,
Brokers and Adjusters"

91. J. R. Breithaupt, Q.C., M.P.P.,
Reply to Hon. Larry Grossman with Select Committee Comments on
Item 93
92. Jan Beerens, Director, Membership Services,
Ontario Trucking Association, Aims and Objectives, and I.A.O. letter
re dump truck insurance rates
93. Daniel Damov, President, I.B.C.,
"Response by I.B.C. to the First Report of the Select Committee"
94. Bruce MacMillan, Executive Director, M.M.I.C.,
Motorcycle and Moped Insurance in Ontario
95. Norman Bortnick, past General Manager, I.C.B.C.,
Summary of Speech, "How the Insurance Corporation Works in Brit-
ish Columbia"
96. Lear P. Wood, Office of the Superintendent of Insurance,
Memo: "Analysis of Woods, Gordon Efficiency Measures in Their
Report IX"
97. Lear P. Wood, Office of the Superintendent of Insurance,
Memo: "The Need for a Greater Government Presence in the Deter-
mination of Auto Insurance Rates in Ontario"
98. Wells McArthur,
"The Green Book; Proposal of Changes to Improve It"
99. *Financial Post* Editorial,
"Time to Overhaul Personal Injury Law", February 4, 1978
100. Globe and Mail,
"Quebec Insurers Scrambling to Conform to Government's No-Fault
Plan by March 1", February 21, 1978, p. B6
101. Colin Atkinson,
"The Experience in Enforcing Compulsory Insurance in the U.K."
102. R. B. Caton,
The Allstate "Catastrophies" emergency programme
103. Insurance Bureau of Canada,
Intercompany Settlement Chart; with explanation
104. Lear P. Wood, Office of the Superintendent of Insurance,
Memo: "A Proposal for Automatic First Party Property Damages and
Loss of User Protection"
105. Dr. Frank Davis and Martin Applewick,
Van Pool Insurance—New Classifications
Worker's Compensation Coverage of Employer-sponsored Van Pools

106. Warren Potter,
 "Drivers Still Pay Heavily for Minor Offences", *Toronto Star*, January 5, 1978
107. William G. Star,
 Comments on the Facility Association, the Wording of The Accident Benefits Section, and the "Actual Cash Value" Problem
108. Swiss Reinsurance,
International Survey of Regulations Governing Motor Insurance, November 1977
109. Insurance Bureau of Canada,
 "The Enforcement of Compulsory Insurance: Reply to the Committee"
110. Insurance Bureau of Canada,
 Distribution of Automobile Third Party Limits: Table
111. Insurance Bureau of Canada,
 Guidelines for Handling Non-Renewals: Notes
112. Government of Ontario, Letters,
 Comments from Ministries on the First Report on Automobile Insurance: Letters from the Attorney General of Ontario, Minister of Transportation and Communications, Solicitor-General of Ontario
113. United Kingdom,
 Press Notice: Royal Commission on Civil Liability and Compensation for Personal Injury, March 16, 1978
114. Independent Insurance Agents of Michigan,
 "The Residual Insurance Market in Michigan: A Plan to Deal With It," March 2, 1978.
115. Royal Commission on Civil Liability and Compensation for Personal Injury, Chairman: Lord Pearson, *Report, Volume One, Volume Two—Statistics and Costing, Volume Three—Overseas Systems of Compensation*, London: Her Majesty's Stationery Office, March 1978.

REFERENCE REPORTS FROM THE COMMITTEE'S CONSULTANTS, WOODS, GORDON & CO.*

March 1977

- Report I The Motor Vehicle System
- Report II Financial Structure of the Automobile Insurance Industry in Ontario
- Report III Determining Automobile Insurance Premiums
- Report IV Processing of Claims by the Insurance Industry
- Report V The Reparations System

January 1978

- Report VI Implementing Compulsory Automobile Insurance
- Report VII Automobile Accident Compensation: The No-Fault Approach
- Report VIII A Government Presence in Rate Regulation
- Report IX Government Ownership of Automobile Insurance
- Report X Review of Marketing, Administration and Claims Adjusting Costs
- Report XI Solvency and Liquidity Rules
- Report XII Responsibilities and Operations of the Superintendent's Office
- Report XIII Standardizing Rating Classifications

* These Reports will be placed in the Legislative Library together with copies of the Committee's Reports.

APPENDIX D
(referred to in Chapter 1)

LIST OF SELF-INSUREDS

Abitibi Provincial Inc.

Air Canada

Bell Canada

Canadian National Railway Company

Canadian National Telegraph Company

Canadian National Transportation Limited

Canadian Pacific Airlines Limited

Canadian Pacific Express Ltd.

Canadian Pacific Transport Company Limited

Chalut Transport (1974) Inc.

Chapman Transport Limited

Deluxe Transportation Limited

East-West Transport Ltd.

Grand River Railway Company

Somerville Car and Truck Rentals Ltd.

In Respect of Vehicles Leased to Canadian Pacific Limited

Gelco Corporation of Canada Ltd.

In Respect of Vehicles Leased to Canadian Pacific Limited

Cronin Transport Limited

Hoar Transport Limited

Husband Transport Limited

Midland Superior Express Limited

Norman's Transport Limited

Provincial Tankers Limited

Smith Transport Co. Limited

Smith Transport (International) Limited

Sudbury Bus Lines Ltd.

The Toronto-Peterborough Transport Company Limited

Toronto Star Limited

Ustel Leasing (Smith Falls) Ltd.

In Respect of Vehicles Leased to Canadian Pacific Limited

March 9, 1978

Ministry of Transportation and Communications

Agents Issuing Section

SURVEY OF VEHICLE INSURANCE COVERAGE OF
GOVERNMENT, CROWN AND
CORPORATIONS IN ONTARIO
(February 1978)

	Number of Vehicles	Liability	Coverage Collision	Deductible	Comments
1. Metropolitan Toronto	1,200	\$10 million but not extended to annual aggregate of \$500,000	Yes, on all department police cars.	Collision and comprehensive of \$1,000	Part of general liability policy, which also covers all vehicles number about 600 vehicles.
2. City of Toronto	1,469	\$1 million fleet	\$25,000 coverage on any one occasion	\$250 deductible on collision	Includes fire department and sundry vehicles.
3. North York	300+	\$1 million fleet	Covered	\$1,000 on collision	
4. Ontario Government	13,000	\$1 million fleet	Self-insure	N/A	Coverage for 20 ministries and commissions. Only exclusions are Ontario Hydro, the Workmen's Compensation Board, and the Liquor Control Board. Presently tendering insurance; coverage may increase.
5. Ontario Hydro	4,700	\$2 million fleet	Self-insure	N/A	
6. Workmen's Compensation Board	135	\$1 million fleet	Self-insure	N/A	Includes affiliated safety associations.
7. Liquor Control Board	200	\$2 million fleet	Insure for collision and comprehensive	\$100 deductible	
8. Federal Government	4,400	Self-insure	Self-insure	N/A	Generally, all government departments and agencies self-insure. This includes several departments including Canada, the Post Office, and Defence Canada.
9. Canadian Broadcasting Corporation	?	\$1 million	Self-insure	N/A	Major crown corporations such CBC, Air Canada, St. Lawrence Seaway, CN, are excluded from the government self-insurance policy and conduct their own policy on insurance.
10. Canadian National Railways	1,000	Security provided	Self-insure	N/A	

APPENDIX F

(referred to in Chapter 1)

POLICE AUTHORITY TO STOP VEHICLES AND DEMAND PROOF OF AUTOMOBILE INSURANCE COVERAGE

As the text of Chapter 1 has indicated, there will always be uninsured vehicles on the road, regardless of the compliance procedures that are introduced. As a result, it will always be important for the law to make appropriate provision with regard to the authority of the police to stop vehicles and to demand proof of insurance.

The Present provisions are set out in Section 3 of the Motor Vehicle Accident Claims Act (R.S.O. 1970 chapter 281 section 3, as amended by Statutes of Ontario 1973 chapter 13 section 2). These provisions are as follows:

- 3.“(1) Subject to subsection 4, the owner of a motor vehicle who operates or permits the operation of the motor vehicle on a highway shall, upon the request of a constable or an officer appointed for carrying out the provisions of The Highway Traffic Act, produce evidence that,
- (a) the vehicle is an insured motor vehicle; or
 - (b) the uninsured motor vehicle fee has been paid in respect of the motor vehicle;
- (2) The Registrar shall issue to the owner of an uninsured motor vehicle a document that may be produced as evidence under subsection 1 that the uninsured motor vehicle fee has been paid in respect of the motor vehicle. 1961-62, c. 84, s. 3(1, 2).
- (3) Every owner of a motor vehicle who fails to produce evidence under subsection 1 when requested to do so or within seventy-two hours of such request is guilty of an offence and on summary conviction is liable to a fine of not less than \$50 and not more than \$500.
- (4) Every owner of a motor vehicle who produces false evidence when he is required to produce evidence under subsection 1 is guilty of an offence and on summary conviction is liable to a fine of not less than \$50 and not more than \$500, and in addition his licence may be suspended for a period of not more than one year. 1970, c. 113, s. 3.
- (5) Where the owner of a motor vehicle is convicted of an offence under subsection 3 or 4 and he has not paid the uninsured motor vehicle fee for the current year in respect of such motor vehicle, he may be required to pay such fee unless he produces evidence that

the motor vehicle was insured at the time the offence was committed.

- (6) Subsections 1, 3, 4 and 5 do not apply to the owner of a motor vehicle that is registered in a country, state or province other than the Province of Ontario. 1964, c. 66, s. 3."

In order for effective police investigations to be conducted, it is essential that police officers have the necessary authority to enable them to carry out their duties. In the case of investigations that are conducted for the sole purpose of ascertaining whether there has been compliance with a compulsory insurance rule, an investigating officer requires the authority to take at least two separate steps:

- (a) to order a driver to stop, solely because he wishes to interrogate him as to whether the appropriate insurance coverage is in force; and
- (b) to interrogate the driver after he has stopped and to require him to answer.

If it is important that a police officer be provided with the legal authority to carry out both of these steps, it is also important that his authority be expressed in terms that are clear and unambiguous. It has been suggested that when a Legislature intends to grant the police the power to limit the citizen's freedom of action, that intention should be expressed in clear and unambiguous terms and should not be left to be inferred from the related terms of a statute. If this condition is applied to the Motor Vehicle Accident Claims Act, it becomes apparent that Section 3 does not *expressly* grant police officers the authority to order a driver to stop for the sole purpose of conducting an insurance interrogation; it only requires that the requisite evidence be produced after the request is made. It is arguable that the intention of the Legislature had been to authorize the officer to order the driver to stop, but it may also be arguable that the intention of the Legislature was to authorize the request to be made only where the driver is already stopped and available.

Some authorities have insisted that the authority to order the driver to stop for this sole purpose is implicit in the authority to request the requisite evidence. On the other hand, there is some indication that in practice police forces prefer to rely upon their authority to stop drivers for the purpose of making safety checks and then, after the vehicle is stopped, to request the appropriate insurance information as an incident to the safety check itself.

It is relevant to examine the corresponding provisions of the Highway Traffic Act, as to safety checks. Section 55 provides as follows:

- "55.(1) Every constable and every officer appointed for the purpose of carrying out the provisions of this Act may require the

driver of any motor vehicle or motor assisted bicycle to submit such motor vehicle or motor assisted bicycle together with its equipment and trailer attached thereto, to such examinations and tests as the constable or officer may consider expedient.”

EXHIBIT 1
STATISTICAL DATA ON THE FACILITY
(Ontario Statistics only for private passenger excluding Motorcycles and Snow Vehicles)

A. Reasons for Transfers to the Facility	1971	1972	1973	1974	1975	1976
1. Under age 21—licenced one year or more	8.4%	8.6%	8.4%	7.9%	7.4%	7.5%
2. "Morals"	8.8	10.2	10.4	9.9	9.1	10.3
3. Liquor or drugs	6.0	5.0	3.9	3.2	3.0	3.0
4. Sports car	3.5	2.9	2.5	2.0	1.7	1.7
5. Condition of auto	3.4	3.0	3.0	2.7	2.1	2.1
6. Licenced less than 1 year—all ages	10.4	11.4	12.5	11.8	11.5	10.4
7. Physical impairment	2.1	2.0	1.9	1.8	1.6	1.7
8. Conviction or accident record	40.9	39.1	38.3	39.2	39.5	37.2
9. Age over 70	12.2	13.0	12.9	12.9	14.1	15.0
10. Not stated	4.3	4.8	6.2	8.6	10.0	11.1
	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>
Vehicle years' liability in Facility— all coverage combined	140,654	161,104	166,672	175,116	185,776	198,573
Total vehicle years' liability—all companies	<u>2,232,403</u>	<u>2,365,906</u>	<u>2,493,805</u>	<u>2,642,126</u>	<u>2,755,563</u>	<u>2,886,779</u>
Percentage of Facility to Total	<u>6.3%</u>	<u>6.8%</u>	<u>6.7%</u>	<u>6.6%</u>	<u>6.7%</u>	<u>6.9%</u>
Percentage of total Facility business subject to surcharge		<u>30.4%</u>	<u>27.5%</u>	<u>27.1%</u>	<u>28.3%</u>	<u>27.1%</u>

APPENDIX G

(referred to in Chapter 2)

TRANSFERS TO THE FACILITY* 1971-1976

One means by which the "high-risk" or residual market is served at present is through the Facility. All automobile insurers in Ontario are subscribers to the Facility and can transfer to it 85% (in a few cases, 100%) of the risk on all policies for which they feel the risk is greater than warranted by the premium. Matters concerning the operation of the Facility were covered in some detail in Appendix E of the Committee's First Report.¹

The Facility is now the third largest automobile insurer in Ontario with gross premiums of \$66.3 and \$81.3 million in 1975 and 1976 respectively.

Exhibit 1 summarizes data concerning private passenger transfers to the Facility for the six years 1971-1976. During this period the number of vehicle years' liability transferred has increased from about 140,000 to almost 200,000. However, as a percent of the total vehicle years' insured in the Province, the percent of Facility business has remained almost constant ranging from 6.3% of the total in 1971 to 6.9% in 1976 and averaging about 6.7% throughout. Likewise, there has been no drastic variation in the reasons for transferring business to the Facility over the period. The main reason for transfers is given as "conviction and accident record", and accounts for about 39% of the total each year. "Over age 70" is the second most common reason for transfers and shows a fairly steady annual increase throughout the period of 15% in 1976.

As previously noted, most transfers to the Facility are written at the normal rates the company uses for each particular class and driver record. Surcharges are only added to the standard manual premium in the case of poor accident and driving conviction records. Throughout the period 1971 to 1976, the percentage of the total Facility private passenger business subject to surcharge has been a fairly constant 27.5% except for 1972 when 30.4% of the transfers were surcharged.

The table covers only private passenger vehicles and excludes commercial vehicles, motorcycles and snowmobiles. For 1976 a summary of

* Extract from Report VI to the Committee from Woods, Gordon & Co., its consultants
1. Select Committee on Company Law, *First Report on Automobile Insurance*, pages 307-314.

the total “population” of the Facility was approximately (in vehicle years’ liability):

Private passenger vehicles	198,500	79.4%
Motorcycles and snowmobiles	33,800	13.6
Commercial vehicles	<u>13,500</u>	<u>7.0</u>
	249,800	100.0%

The reluctance of insurers to insure motorcycles is indicated by the fact that 66.8% of the 1976 motorcycle population in Ontario was placed with the Facility.

APPENDIX H

(referred to in the Introduction and Part II)

AMENDMENT TO SCHEDULE E OF THE INSURANCE ACT

1. The title and items 1 and 2 of subsection 1 of Schedule E to *The Insurance Act* are revoked and the following substituted therefor:

SUBSECTION 1—MEDICAL, REHABILITATION AND FUNERAL EXPENSES

1. All reasonable expenses incurred within four years from the date of the accident as a result of such injury for necessary medical, surgical, dental, chiropractic, hospital, professional nursing and ambulance service and for any other service within the meaning of insured services under *The Health Insurance Act* and for such other services and supplies which are, in the opinion of the physician of the insured person's choice and that of the Insurer's medical advisor, essential for the treatment, occupational retraining or rehabilitation of said person, to the limit of \$25,000 per person.
 2. Funeral Expenses incurred up to the amount of \$1,000 in respect of the death of any one person.
2. Subsection 2 of the said Schedule is revoked and the following substituted therefor:

SUBSECTION 2—DEATH BENEFITS AND LOSS OF INCOME PAYMENTS

Part I—Death Benefits

- A. Subject to the provisions of this Part, for death that ensues within 180 days of the accident or within 104 weeks of the accident if there has been continuous disability during that period, a payment—based on the status at the date of the accident of the deceased in a household where a spouse or dependents survive—of the following amounts:

Head of the Household	\$10,000
Spouse of the Head of the Household	\$10,000
Dependant within the meaning of sub-subparagraph (b) of subparagraph 3 of paragraph B	\$2,000

In addition, with respect to death of the head of the household, where there are two or more survivors—spouse or dependants—the principal sum payable is increased \$1,000 for each survivor other than the first.

B. For the purposes of this Part,

(1) "Spouse of the head of the household" means the spouse with the lesser income from employment in the twelve months preceding the date of the accident.

(2) "Spouse" means either of a man and woman who,

(a) are married to each other;

(b) are married to each other by a marriage that is voidable and has not been voided by a judgement of nullity; or

(c) have gone through a form of marriage with each other, in good faith, that is void and are cohabiting or have cohabited within the preceding year,

and includes,

(d) either of a man and woman not being married to each other who have cohabited,

(i) continuously for a period of not less than five years, or

(ii) in a relationship of some permanence where there is a child born of whom they are the natural parents, and have so cohabited within the preceding year.

(3) "Dependant" means,

(a) the spouse of the head of the household who resides with the head of the household;

(b) a person,

(i) under the age of 18 years who resides with and is principally dependent upon the head of the household or the spouse of the head of the household for financial support,

(ii) 18 years of age or over who, because of mental or physical infirmity, is principally dependent upon the head of the household or the spouse of the head of the household for financial support, or

(iii) 18 years of age or over who, because of full-time attendance at a school, college or university, is principally dependent upon the head of the household or the spouse of the head of the household for financial support; or

(c) a parent or relative,

(i) of the head of the household, or

(ii) of the spouse of the head of the household,

residing in the same dwelling premises and principally dependent upon the head of the household or the spouse of the head of the household for financial support.

- (4) The total amount payable shall be paid to a person who is the head of the household or the spouse of the head of the household, as the case may be, if that person survives the deceased by at least 30 days.
- (5) The total amount payable with respect to death where no head of the household or spouse survives the deceased by at least 30 days shall be divided equally among the surviving dependants.
- (6) No amount is payable on death, other than incurred funeral expenses, if no head of the household or dependant survives by at least 30 days.

Part II—Loss of Income

Subject to the provisions of this Part, a weekly payment for the loss of income from employment for the period during which the injured person suffers substantial inability to perform the essential duties of his occupation or employment, provided,

- (a) such person was employed at the date of the accident;
- (b) within 30 days from the date of the accident the injured person suffers substantial inability to perform the essential duties of his occupation or employment;
- (c) no payments shall be made for any period in excess of 104 weeks except that if, at the end of the 104 week period, it has been established that such injury continuously prevents such person from engaging in any occupation or employment for which he is reasonably suited by education, training or experience, the Insurer agrees to make such weekly payments for the duration of such inability to perform the essential duties.

Amount of Weekly Payment—The amount of a weekly payment shall be the lesser of,

- (a) \$140 per week; or
- (b) 80 percent of the insured person's gross weekly income from employment, less any payments for loss of income from employment received by or available to such person under,
 - (i) the laws of any jurisdiction, and
 - (ii) wage or salary continuation plans available to the person by reason of his employment,but no deduction shall be made for any increase in such payment due to a cost of living adjustment subsequent to the insured person's substantial inability to perform the essential duties of his occupation or employment or for the first two weeks of such substantial inability.

For the purpose of this Part,

- (1) there shall be deducted from an insured person's gross weekly income any payments received by or available to him from part-time or other employment or occupation subsequent to the date of the accident;
 - (2) a principal unpaid housekeeper residing in the household not otherwise engaged in occupation or employment for wages or profit, if injured, shall be deemed disabled only if completely incapacitated and unable to perform any of his or her household duties and, while so incapacitated, shall receive a benefit at the rate of \$70 per week for not more than 12 weeks;
 - (3) a person shall be deemed to be employed,
 - (a) if actively engaged in an occupation or employment for wages or profit at the date of the accident; or
 - (b) if 18 years of age or over and under the age of 65 years, so engaged for any six months out of the preceding 12 months;
 - (4) a person receiving a weekly payment who, within 30 days of resuming his occupation or employment is unable to continue such occupation or employment as a result of such injury, is not precluded from receiving further weekly payments;
 - (5) except for the first two weekly of disability, where the payments for loss of income payable hereunder, together with payments for loss of income under another contract of insurance other than a contract of insurance relating to any wage or salary continuation plan available to an insured person by reason of his employment, exceed the actual loss of income of the insured person, the Insurer is liable only for that proportion of the payments for loss of income stated in this policy that the actual loss of income of the person insured bears to the aggregate of the payments for loss of income payable under all such contracts.
3. Subsection 3 of the said schedule is revoked and a subsection titled SUBSECTION 3—UNINSURED MOTORIST COVER is substituted therefor. (The provisions of the new subsection 3 are not reproduced here.)
 4. A new subsection titled SPECIAL PROVISIONS, DEFINITIONS AND EXCLUSIONS OF SECTION B is included, incorporating the provisions of the former subsection 3 with certain substitutions. (The provisions of this subsection are not reproduced here.)
 5. This Regulation comes into force on the 1st day of July, 1978.

APPENDIX I

(referred to in Chapter 11)

SOLVENCY AND LIQUIDITY RULES*

THE PRESENT RULES

The present “in-house” rules used by the Superintendent’s Office were discussed briefly in the Committee’s First Report.¹ These are explained in further detail in this section as follows:

1. Premiums to capital and surplus.
Net premiums written should not exceed twice the capital and surplus (i.e. policyholders’ surplus or shareholders’ equity).
2. Dividend restriction.
No company shall pay dividends to shareholders which exceed 50% of its previous years after tax profit.
3. Unearned premiums to capital and surplus.
Unearned premiums on a 100% basis should not exceed capital and surplus.
4. Admitted assets to adjusted liabilities.
Total admitted assets (at market values) must amount to at least 115% of total adjusted liabilities with unearned premiums on a 100% basis.
5. Net retention rule.
A company’s net risk retention on any one policy should not exceed 2% of capital and surplus.

Exhibit 1 outlines the calculations made to ensure compliance with these rules. The financial information is taken from the “sample” financial statements of a hypothetical insurer, A.B.C. Insurance Company, which are presented as Exhibit 2.

While the accounting concepts and terminology utilized by the general insurance industry were outlined in Woods, Gordon & Co.’s Report II to the Committee, definitions of the applicable terms with respect to the solvency and liquidity tests are reiterated below:

- 1) Unearned premium reserve.

This is represented by the portion of premiums which are held in trust by the company and are not yet earned because the policyholders have not yet received the full term of protection for which the premium was collected.

* Extract from Report XI to the Committee from Woods, Gordon & Co., its consultants.

1. The Select Committee on Company Law, *First Report on Automobile Insurance*, 1977, Pages 195 & 196.

EXHIBIT 1

SOLVENCY TEST CALCULATIONS
FOR ABC INSURANCE COMPANY
(See Exhibit 2)

1. *Net Premiums to Capital and Surplus (2:1)*

Net Premium Revenue Per Financial Statements	\$3,000,000
Add Unearned Premium Increase in Year	200,000
Net Premiums Written	<u>\$3,200,000</u>
Capital and Surplus	<u>\$1,700,000</u>
Ratio = $\frac{\text{Net Premiums Written}}{\text{Capital and Surplus}}$	$\frac{3,200,000}{1,700,000}$
	= 1.88:1

2. *Dividend Restriction*

After Tax Profit	<u>\$ 250,000</u>
The maximum dividend that ABC insurance company is allowed to pay is (50% of \$250,000) \$125,000 in the coming year.	

3. *Unearned Premiums to Capital and Surplus (1:1)*

Unearned Premiums on a 100% basis	\$1,600,000
Total Shareholders' Equity	<u>1,700,000</u>
Ratio = $\frac{\text{Unearned Premiums}}{\text{Shareholders' Equity}}$	$\frac{1,600,000}{1,700,000}$
	= .94:1

4. *Admitted Assets to Adjusted Liabilities (115%)*

Assumptions:	
—no reserve for reinsurance ceded to unregistered companies	
—no deposits from reinsurers	
—all assets are admitted assets	
Total Liabilities	<u>\$3,400,000</u>
Total Assets	<u>\$5,100,000</u>

Test

115% of Total Liabilities	\$3,910,000
Total Admitted Assets at Market Values	<u>5,100,000</u>
Excess of Admitted Assets Over 115% of Total Liabilities	<u>\$1,190,000</u>

5. *Net Retention Rule*

The net retention rule which relates to risk retention on each policy can only be checked in a detailed examination of the company's affairs. With its present shareholder's equity, the company would not be able to retain a risk for over \$34,000 on any one policy.

EXHIBIT 2
ABC INSURANCE COMPANY
FINANCIAL STATEMENTS
For the year ended December 31, 1977

BALANCE SHEET
Assets

Cash	\$ 100,000
Investments	4,500,000
Amounts Receivable	350,000
Other Assets	150,000
Total Assets	<u>\$5,100,000</u>

Liabilities and Shareholders' Equity

Liabilities:	
Amounts Payable	\$1,800,000
Unearned Premiums on a 100% Basis	1,600,000
Total Liabilities	<u>\$3,400,000</u>
Shareholders' Equity:	
Capital	1,000,000
Surplus	700,000
Total Shareholders' Equity	<u>1,700,000</u>
Total Liabilities and Shareholders' Equity	<u>\$5,100,000</u>

INCOME AND RETAINED EARNINGS

Net Premium Revenue	\$3,000,000
Deduct Expenses	2,900,000
Underwriting Profits	100,000
Investment Income	350,000
Income Before Tax	450,000
Income Taxes	200,000
Net Income After Tax	250,000
Opening Balance of Surplus	450,000
Closing Balance of Surplus	<u>\$ 700,000</u>

2) Unearned premiums on a 100% or 80% basis.

The Office of the Superintendent requires companies to write off as incurred the costs of selling to a policyholder and of issuing a policy to him. Since the premiums are earned over the term of the policy it is reasonable to assume that the costs should also be allocated over the policy period in order to match premium income and costs in measuring profitability. Unearned premiums on a 100% basis would be the full unearned premium as described in (1) above; unearned premiums on an 80% basis would indicate that 20% of the unearned premiums have been taken into income, to offset the immediate write-off of the selling costs of acquiring a policyholder and the costs of issuing the policy. The 20% cost factor is an estimate.

3) Shareholders' Equity.

This amount is the capital plus the surplus of a company. It has also been described as assets less liabilities, net assets or policyholders' surplus.

4) Admitted Assets.

To provide adequate protection for policyholders, it is considered necessary that an insurer incorporated in Ontario maintain assets (total admitted assets) that could be converted relatively easily, into cash.

Generally, assets are recorded at conservative values. As a result, furniture and fixtures, inventories of supplies, deferred premium acquisition costs and similar items which would normally be considered "assets" are not valued by the insurance industry but rather are written off to expense when acquired. The remaining assets are referred to as admitted assets.

BACKGROUND AND PURPOSE OF THE PRESENT RULES

The origin of many of the formulae used to measure the financial strength of insurance companies most likely can be attributed to a publication—"Fundamentals of Fire and Casualty Insurance Strength"—written in 1949 and subsequently updated in 1955 by Roger Kenney. This United States publication was designed to enable the policyholder and investor to analyze the financial strength of fire and casualty insurance companies. While Kenney did not originate all of the procedures, it is generally acknowledged that his studies either provided or solidified the logic and rationale which continue to provide support for their use today in both Canada and the United States. A more detailed consideration of the justification for and intent of each rule follows:

1. Premiums to Capital and Surplus

The Superintendent's Office has an in-house rule that the business a company can safely write should be limited to twice its capital and surplus.

The theory behind a restriction in this area is that each dollar of premium written exposes a company to a potential loss. This ratio is designed to ensure that (a) the company's growth is adequately supported with investments by its owners, (b) the company is not taking on excessive potential liabilities and (c) future stability and liquidity is not hindered by rapid expansion.

Roger Kenney established the "2 for 1" rule back in the mid 1930's by performing a thorough analytical study of the difficulties encountered by certain insurance companies. Financial difficulties were precipitated by sharply mounting loss ratios accompanied by a sharp decline in the securities markets. Kenney's study led him to the conclusion that in a majority of the cases the "venturesome area was entered when a company's premium volume began to exceed \$2.00 for every dollar of policyholders' surplus".

In the late 1930's New York State included this ratio in its first draft of changes to its Insurance Code. Decisions made in New York State in this

period had national implications such that this arbitrary "2 for 1" rule has been used in many jurisdictions. However, it is not included in legislation in any other jurisdiction for a number of reasons including:

- The ratio sets out too definite a pattern for casualty company growth.
- No allowance is made for the class of business, the territory or term of the policies written.
- Volume is not the major reason for creating unstable financial conditions in a company; indiscriminate writing is perhaps the major reason.

It is argued, therefore, that a subjective evaluation of the status of each company must be made in addition to the calculation of this ratio.

2. Dividend Restriction

This rule is an extension of the "2 for 1" rule and is designed to protect the base of shareholders' equity and to restrict the possibility of large immediate withdrawals of capital or surplus which may hinder the financial stability of a company.

Since casualty insurance companies are in a position where they must estimate deferred liabilities for unsettled and also unreported claims, retention of capital and surplus may be required to provide a margin of safety for errors in estimation of these liabilities.

The restriction which is included in the New York State legislation with respect to the payment of dividends by domestic casualty and surety companies reads as follows:

"No dividend is to be paid by these companies if the dividend, together with any dividend paid in the preceding twelve months exceeds the lesser of 10% of the company's earned and paid-in surplus or 100% of its "adjusted net investment income" unless the Superintendent of Insurance has given his prior approval."¹

It is difficult to prove whether specific dividend restrictions, such as the 10% of earned and paid-in surplus as in New York State, or 50% of previous years after tax profit as in Ontario, are the correct restrictions. However, it does seem reasonable that some restriction be placed on dividends in order to provide an adequate base of shareholders' surplus and that the designated restriction be included in legislation.

3. Unearned Premiums to Capital and Surplus

The in-house rule that unearned premiums on a 100% basis should not exceed capital and surplus is a refinement of the "2 for 1" premium to equity ratio test.

1. *The Insurance Law of New York State*, Section 313.

This ratio for determining "Fire Insurance Strength" was developed by Kenney in the mid 1930's. Kenney explains that the unearned premium reserve is a measure of the outstanding potential liability of the company in the form of risks accepted. Thus, the larger the cushion of safety provided by shareholders' equity in excess of unearned premiums, the greater the strength of the organization. In addition to this ratio, Kenney mentions that the quality and stability of shareholders' equity must be considered. The quality is determined by the types of assets the company holds. The stability is largely dependent upon the risks that are assumed and the resulting accurate measurement of loss reserves.

The accounting principles applied by each company will also be a factor in determining the criteria for assessing the results of this test. Some companies follow the full term reporting method of accounting. The unearned premium for the full term of the policy, even in excess of one year, will be recorded as a liability regardless of whether payment has been received. Others follow the annual reporting method of accounting, wherein only the unearned premium on annual instalments will be shown as a liability. Companies following the annual reporting method will show lower unearned premiums than full term reporting companies and thus a more favourable unearned premium to capital and surplus ratio.

The ratio is relevant for fire insurance companies because the settlement of losses is reasonably prompt. With reasonably prompt settlement, unearned premiums can be related to anticipated losses. However, according to figures which Kenney quotes from casualty insurance companies, about two-thirds of the liability loss reserves and three-quarters of the workmen's compensation loss reserves are related to business written in years preceding the current year. Because of the deferred liability nature of casualty insurance company operations, the adequacy of loss reserves and the lawsuit record of the company are the crucial measurements for this segment of the industry.

Since four to five years are required to settle many of the claims against casualty insurance companies, it does not appear that the unearned premium to capital and surplus ratio is totally meaningful for this type of insurer. More relevant are examinations of the adequacy of loss reserves and the lawsuit experience of casualty insurance companies, matters which are examined by the Superintendent's Office during the annual financial examination. The detailed nature of such reviews and the need for judgmental decision based upon the specific circumstances render the legislation of this more applicable rule to be difficult.

4. Admitted Assets to Adjusted Liabilities

Admitted assets, at market values, must amount to at least 115% of total adjusted liabilities with unearned premiums on a 100% basis. This "in

EXHIBIT 3
AMENDMENT TO CANADIAN AND BRITISH INSURANCE
COMPANIES ACT AND THE FOREIGN INSURANCE
COMPANIES ACT

Assets, Minimum Amount

"103. (1) Subject to subsections (1.1) to (1.19), a company shall maintain assets, exclusive of any investments of the company that are not authorized by this Act or were not authorized by law at the time of their acquisition, the total value of which, when determined on the same basis as is prescribed under this Act for the purposes of the annual statement of the company, or on the basis of the market values of such assets, whichever basis produces the greater total value, is at least equal to the aggregate of the following amounts:

- a) an amount equal to the reserve computed in accordance with paragraph 102(1)(a) for non-cancellable accident and sickness policies, and for claims under accident and sickness policies payable in instalments;
- b) an amount equal to 1.15 times the amount of the unearned premiums in respect of the policies other than the policies referred to in paragraph (a);
- c) an amount equal to 1.15 times the amount of the provision for claims incurred but unpaid, other than claims referred to in paragraph (a); and
- d) an amount equal to the total of the other liabilities of the company.

house" rule is similar to the federal rule that is contained in legislation. The federal act has recently been revised, as illustrated in Exhibit 3, to require 115% over certain liabilities and 100% over other liabilities. The excess of admitted assets is intended to provide adequate protection for policyholders. The assets are to be in a form that can be converted relatively easily into cash to extinguish liabilities including an adequate reserve for the business ceded with unlicensed reinsurers.

It is uncertain how this rule was established as an accurate safeguard against loss in the event of insolvency. The Superintendent of Insurance of Ontario is of the opinion that the percentage of 115% was arbitrarily chosen as a conservative guideline to provide a margin of safety.

5. Net Retention Rule

The general guideline used by the Superintendent's Office provides that a company's net retention of any one risk should not exceed 2% of its capital and surplus. Without such a restriction, one large claim could quickly render a company insolvent. Concentration of coverage in a certain area causes a similar concern in that one disaster could affect a large number of policies. This problem would pertain more to other lines of general insurance and to life insurance rather than to auto insurance. The safeguards provided by the net retention rule and the ratio of premiums to shareholders' equity are intended to prevent strain on a company's financial position in these instances.

The present net retention rule means that a company with a capitalization of \$1,000,000 would not be able to retain a policy entirely for its own account over \$20,000. In order to cover a \$1,000,000 risk the insurer would require shareholders' equity of \$50,000,000.

New York State has a net retention rule which allows a company to write up to 10% of its capital and surplus on any one risk and Quebec in its new legislation has adopted the same percentage. The Chief Examiner in Ontario is of the opinion that allowing net retentions of up to 10% of shareholders' equity is too high because losses on only ten risks would render a company technically insolvent.

There might be merit in legislating the net retention rule to protect the insured from insolvency of an insurer. A subjective evaluation is required to determine what a reasonable retention percentage for each policy should be.

PRESENT ENFORCEMENT MECHANISMS

The financial affairs of each Ontario incorporated company are reviewed annually by the examiners in the Superintendent's Office. If a company does not comply with any of the above in-house tests, a meeting is held with the management of the company to determine the reasons for the failure. Generally, a programme is worked out with management to rectify the problem.

If the programme fails to have the desired effect or if management refuses to implement a programme acceptable to the Superintendent, a report on the affairs of the company is made to the Minister. A hearing is held and as a last resort, a company's licence may be suspended. The company does have a right of appeal to the Supreme Court. On suspension of a company's licence, the Superintendent does have the power to seize assets and wind-up the company.

Probably the shortest time span between the meeting with the company's management and the suspension of a company's licence, if an appeal is involved, is one year. During this period, the company can still transact business in its normal fashion subject to the close scrutiny of the Superintendent's Office.

APPENDIX J

(referred to in Chapter 11)

RESPONSIBILITIES AND OPERATIONS OF THE SUPERINTENDENT'S OFFICE*

HISTORY

Regulation over insurance companies commenced in Ontario prior to Confederation. The business of insurance in this period was on a comparatively small scale and thus such regulation was of a very simple nature. According to the first known report of the Superintendent in 1880, insurance companies in this early period dealt mainly in fire and accident insurance and only one company handled life insurance.

In 1870 the Ontario Legislature provided that all companies without a Dominion licence should secure one from the Provincial Treasurer, make deposits, file annual reports and submit to inspection. In the same year, an Ontario statute required all fire insurance companies doing business in the Province to insert certain prescribed terms and conditions in their policies. In later years, similar terms and conditions were required for other types of insurance. By 1879, Ontario had an Inspector of Insurance. By 1914, a provincial insurance department headed by a Superintendent had been established, and regulatory machinery similar to that of the Dominion had been set up.

Originally the Superintendent's position was called the Inspector of Insurance Companies under the Public General Act—Relating to Insurance (1877). The Inspector of Insurance Companies was entrusted with the responsibility to present yearly statements of insurance companies to the Treasurer and to ensure that the companies' statement of affairs showed the companies' ability to meet their liabilities prior to renewal of licences. In addition, the Inspector was to visit the head office of each company in Ontario once a year and report to the Treasurer on all matters connected with insurance.

The responsibilities of the Inspector or Superintendent of Insurance were broadened in later years to encompass other industries as various statutes were enacted for other "financial institutions" in Ontario. In addition to the role of Superintendent of Insurance, the Superintendent is also the Executive Director of the Financial Institutions Division of the Ministry of Consumer and Commercial Relations.

* Extract from Report XII to the Committee from Woods, Gordon & Co., its consultants.

RESPONSIBILITIES OF THE FINANCIAL INSTITUTIONS DIVISION

The Financial Institutions Division has administrative responsibilities under the following Provincial Acts:

THE CEMETARIES ACT
THE CREDIT UNIONS AND CAISSES POPULAIRES ACT, 1976
THE GUARANTEE COMPANIES SECURITIES ACT
THE INSURANCE ACT
THE INVESTMENT CONTRACTS ACT
THE LOAN AND TRUST CORPORATIONS ACT
THE MARINE INSURANCE ACT
THE MOTOR VEHICLE ACCIDENT CLAIMS ACT
THE ONTARIO DEPOSIT INSURANCE CORPORATION ACT
THE PREARRANGED FUNERAL SERVICES ACT
THE PREPAID HOSPITAL AND MEDICAL SERVICES ACT

The legislated responsibilities of the Financial Institutions Division are contained in the various acts which it administers. In general terms, the Division is required to monitor the activities of organizations licenced under these acts to ensure that the following minimum requirements are maintained:

1. These companies and associations are capable of meeting their obligations;
2. The individuals working in these industries are knowledgeable, competent and trustworthy; and
3. The industries are being operated in the best interests of the public and there is full and proper disclosure of information to the public.

In addition to the aforementioned responsibilities, this Division provides a policy service division to assist the public in their dealings with insurance companies and administers The Canada Deposit Insurance Corporation Act on behalf of the federal government for loan and trust companies incorporated in Ontario.

A brief summary of the Acts pertaining to automobile insurance follows:

The Insurance Act

The provisions of this Act are intended to ensure that insurance companies licenced to carry on business in the Province of Ontario are capable of meeting their obligations; that those who work in the industry are knowledgeable, competent and trustworthy; and that the industry is operated in the best interests of the public, with full and proper disclosure to the public.

The Act provides certain minimum requirements which must be met by an insurance company seeking a licence to carry on the business

of insurance in Ontario and it also provides for the licencing of agents, brokers and adjusters who must similarly meet certain minimum requirements before they can be licenced.

The parts of the Act dealing with specific classes of insurance provide for various aspects of the contractual relationship between the insurer and the insured and in some cases set out statutory conditions which are deemed to be part of each policy of insurance issued.

The Motor Vehicle Accident Claims Act

The purpose of the Act is to provide that any person who has a cause of action against the owner or driver of an uninsured motor vehicle, in respect of death, personal injury, loss or property damage occasioned in Ontario by an uninsured motor vehicle, may seek compensation for his damages from the Motor Vehicle Accident Claims Fund. The Act provides that the Fund in turn may attempt to recover any monies paid out by it from the person responsible for the damages. The Act sets out the procedures for obtaining payment out of the Fund and the necessary steps to be followed by a claimant.

The Act is administered by the Director of The Motor Vehicle Accident Claims Fund who is appointed under the Act. The Superintendent of Insurance is deemed to be the agent of the owner and of the operator of every uninsured motor vehicle for purposes of service of notice or a process in an action, and also has certain other administrative responsibilities under the Act.

Currently under consideration is an amendment to the Act which will give authority to set agents commission for the collection of uninsured motor vehicle fees.

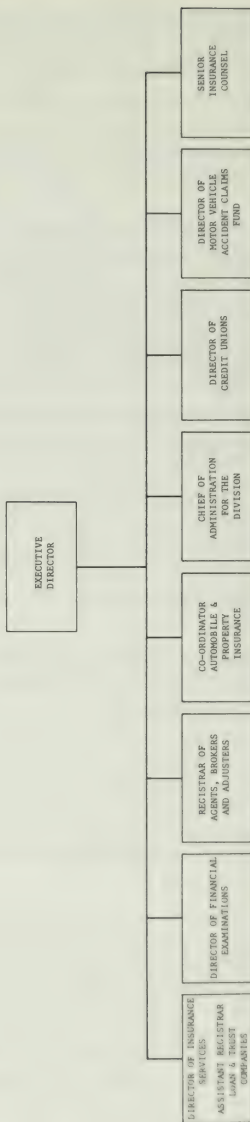
ORGANIZATION

The Financial Institutions Division has been reorganized within the last two years to provide for more appropriate lines of reporting and better segregation of duties. A summary organization chart of the Financial Institutions Division is shown as Exhibit 1.

The summary organization chart is self-explanatory with respect to six of the eight reporting lines to the Executive Director. The functions of the Director of Insurance Services and the Coordinator of Automobile and Property Insurance require more explanation to describe their roles in the Division.

The Insurance Services area reviews the actuarial assumptions utilized by companies to set rates, it insures development of necessary legislation and regulation, licences insurers, investigates consumer complaints and performs special studies.

SUMMARY ORGANIZATION CHART
FINANCIAL INSTITUTIONS DIVISION



The Coordinator of Automobile and Property Insurance provides liaison with industry on various problem areas and prepares or reviews proposed changes to division policy based upon committee reports, legislative proposals, consumer complaints or changes in other jurisdictions. He also provides general consulting advice to the other segments of the division.

Exhibits 2 and 3 provide additional detail with respect to the organization of the Division and the responsibilities of each of the departments. It should be noted that the present span of control of the Superintendent would appear to be reaching the point where his effectiveness in some areas might be impaired by significant additional responsibilities.

STAFFING

The present complement of staff in the Financial Institutions Division is summarized as follows:

Executive director and 2 secretaries		3
Personnel on insurance		
Directors	6	
Others	<u>98</u>	104
Other personnel		
Directors	2	
Others	<u>57</u>	<u>59</u>
Total staff, October 1977		<u><u>166</u></u>

Greater detail on personnel by department is contained in Exhibit 2.

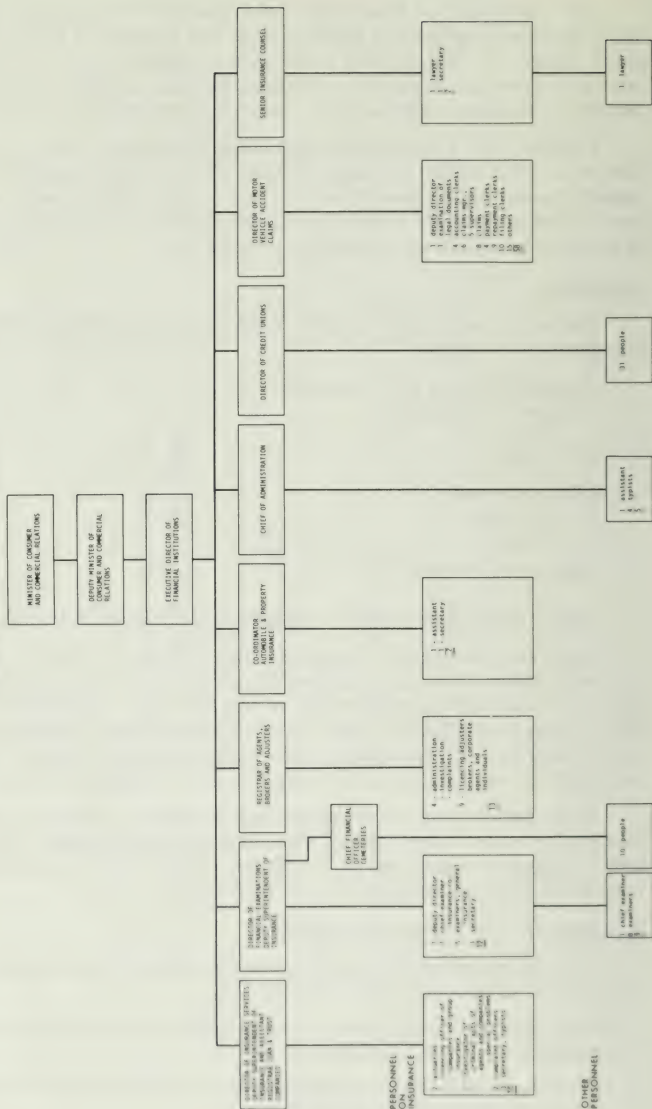
There are a number of changes affecting various Provincial Acts administered by the Financial Institutions Division which will have an impact upon the future staffing requirements of this Division. Amendments have been proposed to the Credit Unions Act, the Loan and Trust Corporation Act and the Insurance Act. In addition, a new electronic payment system for the Federal Borrowers and Depositors Protection Act has been introduced.

At the present time, the Superintendent is unable to accurately predict his complement or numbers of staff required in the future because of the volume of changes proposed and the uncertainty of the scope of recommendations which will result from current studies in process.

POWERS OF THE SUPERINTENDENT

The legal powers of the Superintendent are set out in The Insurance Act and can be described generally as follows:

1. To pass upon the qualifications of and to licence all insurers carrying on business in the Province of Ontario.
2. To require, accept, hold and administer deposits for the protection of Ontario and other Canadian policyholders.



MINISTRY OF CONSUMER AND COMMERCIAL RELATIONS

RESPONSIBILITIES OF DEPARTMENTS OF FINANCIAL
INSTITUTIONS DIVISION RELATED TO INSURANCE

<p>DIRECTOR OF INSURANCE SERVICE (10 people)</p> <ol style="list-style-type: none"> 1. Review of actuarial assumptions of provincially incorporated insurance companies to monitor compliance with the act and reasonableness of rates on existing and new insurance coverage. 2. Ensure development of necessary legislation and related regulations based on: <ol style="list-style-type: none"> (i) trends in industry; (ii) development in other jurisdictions (iii) special studies (iv) re-evaluation of legislative programs in effect. 3. Actuarial service for all sections of the division. 4. Determine where special studies should be made for developing new approaches to existing problems. 5. Handle consumer complaints and requests for assistance in dealing with problems. 6. Liaison with industry on compliance with various Provincial Acts. 	<p>DIRECTOR OF FINANCIAL EXAMINATION (12 people)</p> <ol style="list-style-type: none"> 1. Examination of financial affairs of Ontario incorporated insurance companies and selected agencies to ensure conformity with the Insurance Act. This examination is carried out to ensure that unsatisfactory financial conditions and undesirable practices by regulated companies are promptly detected and corrected. 2. Review of management capabilities of individuals in insurance companies. 3. Review of financial affairs of 10 extra provincial insurance companies. Two audited. 4. Review policy forms and estate and trust areas of federally incorporated insurance companies. 5. Liaison with companies, legal and accounting professions, regulatory authorities both federally and provincially to discuss and review practices and legislation. 	<p>REGISTRAR OF AGENTS, BROKERS AND ADJUSTERS (13 people)</p> <ol style="list-style-type: none"> 1. Manage the licensing program which is responsible for controlling the activities of 25,000 insurance agents, brokers and adjusters. 2. Maintain regulatory control over registrants by ensuring compliance with legislation on standard of conduct, follow-up complaints conducting informal hearings issuing warnings and reprimands and revoke or suspend licences where necessary. 3. Prepare examinations in association with industry representatives, arrange examination centres, mark examinations and lecture at courses. 4. Examine financial statements submitted annually by agents and brokers before issuing licence renewals and liaising with director of financial examinations if an examination is deemed warranted of an agency. 5. Recommend new or revised legislation to the superintendent and assist in its formulation and implementation.
<p>CO-ORDINATOR OF AUTOMOBILE AND PROPERTY INSURANCE (2 people)</p> <ol style="list-style-type: none"> 1. Prepare, review and recommend branch policies based on: <ol style="list-style-type: none"> (i) committee reports; (ii) legislative proposals; (iii) consumer complaints; (iv) policy changes in other jurisdictions. 2. Liaison with industry and other jurisdictions on: <ol style="list-style-type: none"> (i) market practices; (ii) products; (iii) rates. 3. Review market, availability for consumers. 4. Inter ministry consulting. 5. Assist superintendent in dealing with national superintendent committees. 6. General consulting. 	<p>DIRECTOR OF MOTOR VEHICLE ACCIDENTS CLAIMS (58 people)</p> <ol style="list-style-type: none"> 1. Deal with losses to innocent victims caused by motorists who are either uninsured or are unidentified. 2. Manage assets of fund designated for purpose described in Point 1. 3. Arrange for lawyers to assist in the settlement of lawsuits related to uninsured or unidentified motorists. 4. Arrange for payment of claims and look after repayments by uninsured to the fund. 5. Manage reinstatement of licences to motorists who were involved in accidents. 6. Liaison with industry and regulatory bodies on problems and recommend new or revised legislation. 	<p>SENIOR INSURANCE COUNSEL (2 people)</p> <ol style="list-style-type: none"> 1. Provide assistance to other departments of the superintendent of insurance by interpreting statute and reviewing or preparing new legislation. 2. Assist in enforcing statute.

3. To make periodic examinations for solvency purposes of the financial condition of the Ontario and extra-provincial companies licenced.
4. To require annual filings of financial statements by all licenced companies and to prescribe the basis upon which securities listed therein shall be valued for Ontario and extra-provincial companies.
5. To require and compile statistical returns such as fire insurance premiums and losses and automobile insurance loss cost data, for Ontario business only. The Superintendent presently designates The Insurance Bureau of Canada as his agent to perform this task.
6. To compile and issue an Annual Report containing detailed financial statements of all provincial and extra-provincial companies licenced by the Province and a modified financial statement of companies registered under the Dominion Insurance Act, and to include statistical data on the Ontario experience of such companies in respect of premiums and losses in the various classes of insurance.
7. To administer and enforce the provincial laws relating to insurance contracts in Ontario, including preparation of legislation respecting contractual law in insurance matters. General supervision and regulation of the carrying on of the business of insurance within the Province, including approval of policy forms, approval of constitution and by-laws of mutual benefit and fraternal societies and analysis of cost and rates of insurance.
8. To pass upon the qualifications of and licence insurance agents, brokers, and adjusters; to supervise such agents, brokers and adjusters with respect to rebating, handling trust funds, payment of commissions and other matters.
9. To provide services to the public such as investigation of complaints, answering inquiries and requests for information.

The Superintendent does not have the power to take away the licence of companies or to cause companies to cease writing new business if he learns of problems, for example, if he suspects solvency difficulties. Other matters which are relevant to the consideration of the responsibilities and operations the Superintendent's Office are outlined below.

Motor Vehicle Accident Claims Fund

Compliance with and enforcement of compulsory insurance for automobiles will have a significant impact upon the M.V.A.C.F. It has been suggested that the scope of the M.V.A.C.F. would be significantly curtailed with implementation of compulsory insurance. However, the need for this protection would continue and it would be necessary to provide for the victims of hit-and-run drivers and out-of-province drivers and those few motorists who might continue to elude the enforcement mechanisms.

Because of the reduced requirements for the Fund, representatives of the M.V.A.C.F. estimate that their staffing requirements will be reduced by approximately 30 man-years after the implementation has been completed.

Consumer Complaints

Presently, the Superintendent's Office receives numerous complaints and/or requests for assistance from consumers in connection with their disputes with insurance companies. An analysis of enquiries is shown in Exhibit 4. Many of the disputes involve small claims and the consumer is reluctant to take legal action because of the costs of litigation. The Superintendent, of course, does not have any authority to settle these disputes and can only attempt to encourage an amicable settlement between the consumer and the insurer.

EXHIBIT 4 INSURANCE INFORMATION AND COUNSELLING SERVICE ENQUIRIES AND COMPLAINTS

1975

Written enquiries	1,609
Telephone enquiries (estimated)	<u>10,000</u>
Total	<u>11,609</u>

Analysis of Enquiries	Number	Percentage
*Automobile Insurance	5,921	51%
Property Insurance	1,393	12
Accident and Sickness	1,103	9.5
Life Insurance	1,045	9
Marine and General Liability	464	4
General Enquiries	<u>1,683</u>	<u>14.5</u>
	<u>11,609</u>	<u>100.0%</u>

* Most queries involved the settlement of claims, largely resulting from disputes over collision deductibles and substitute vehicle rentals. Individuals and agents requesting assistance with the placement of substandard risks were also a problem. (Information provided by the Superintendent's Office.)

Section 102 of the Insurance Act does make provision for settlement of the amount in dispute through binding arbitration; however, this mechanism is not widely used because of the high cost and the length of time required for a decision.

It has been suggested that a small claims board comprised of representatives of the Superintendent's Office and the industry, or an independent board of arbitrators knowledgeable on insurance matters, could be established to adjudicate these claims. The consumer should maintain the right of appeal to the courts if he continues to be dissatisfied with the ruling and the amount of the claim justifies appeal. Besides providing a hearing for the irate consumer with a very small claim, the number of small insurance claims (including arguments over deductibles) could be reduced in the lower courts.

According to the Superintendent's Office, the practice of many insurers today is to waive their right of offset of the collision deductible and, accordingly, fewer disputes over collision deductibles will be experienced by the small claims courts.

Recent legislation has increased the jurisdiction of the small claims courts from \$400 to \$1,000. It is expected that this court would experience increased activity from automobile insurance claims.

Financial Examinations

As of December 31, 1976, out of 181 organizations licenced or writing automobile insurance in Ontario, only 17 were incorporated provincially and accordingly reported to the Ontario Superintendent for all regulatory requirements. The federal Superintendent, therefore, was responsible for the annual examination and solvency of the other 164 organizations. The Ontario Superintendent, however, was also responsible for such matters as licencing, contracts and premiums for these 164 organizations.

Some of the Provinces such as Manitoba have contracted out their responsibilities for annual examinations and review of solvency of provincially incorporated companies to the Federal Superintendent. The small number of provincially incorporated companies and the parallel functions of the Federal and Provincial Departments of Insurance were the reasons for Manitoba's withdrawal from this area of responsibility.

Rate regulation, which is under provincial jurisdiction, is related to solvency, which, for the majority of companies, is under federal jurisdiction. It may be of importance to the Ontario Superintendent to be able to closely monitor the effect on solvency of changes to licencing, contracts and premiums. On the other hand, the small number of Ontario incorporated companies and their small percentage of automobile business in the Province may offset any benefits which may be derived from continuing to carry out these examinations.

APPENDIX K
(referred to in Chapter 12)

**AUTOMOBILE INSURANCE IN ONTARIO
INDUSTRY OPERATING ANALYSIS*
1974 AND 1975**

The analysis on the table on page 256 represents a further estimated breakdown of the 1974 and 1975 industry results utilizing data obtained from the I.B.C. Expense Allocation and Reporting System for those years.

Operating cost ratios reported by I.B.C. members on a national basis were assumed to be representative of the total industry in Ontario.

Because claims incurred and adjusting and settlement costs charged directly to the claims file were not collected by the I.B.C. system, it has been necessary to continue to assume claims expenses at 11% of premiums earned. Accordingly, claims incurred have been adjusted by the amount necessary to balance to the estimated profit (loss) before income taxes for the Ontario industry.

* Extract from Report X to the Committee from Woods, Gordon & Co., its consultants.

APPENDIX KAUTOMOBILE INSURANCE—ONTARIOINDUSTRY OPERATING ANALYSIS

	1974				1975			
(000's)	\$	% Direct Prem. Writ.	% Net Prem. Earn.	% Direct Claim Payments	\$	% Direct Prem. Writ.	% Net Prem. Earn.	% Direct Claim Payments
Direct Premiums Written	627,236	100.0	101.7	141.8	815,272	100.0	111.4	163.1
Net Premiums Written	635,078			143.6	811,089			162.2
Net Premiums Earned	616,958	98.3	100.0	139.4	731,553	89.7	100.0	146.3
Cost of Acquiring								
Commissions	79,032	12.6	12.8	17.9	100,278	12.3	13.7	20.1
Agent Service & Promotion	10,036	1.6	1.6	2.2	1.3	1.3	1.4	2.1
Allocated General Administration	3,763	.6	.6	.9	4,076	.5	.6	.8
	92,831	14.8	15.0	21.0	144,953	14.1	15.7	23.0
Policy Processing								
Direct Administration	33,244	5.3	5.4	7.5	41,579	5.1	5.7	8.3
Allocated General Administration	12,544	2.0	2.0	2.9	13,860	1.7	1.9	2.8
	45,788	7.3	7.4	10.4	55,439	6.8	7.6	11.1
Claims Settlement								
Direct Payments	442,248	70.5	71.7	100.0	499,943	61.3	68.3	100.0
Legal Costs and	67,865	10.8	11.0	15.3	80,471	9.9	11.0	16.1
Adjuster & Appraisal Costs								
Direct Administration	15,681	2.5	2.6	3.5	21,197	2.6	2.9	4.2
Allocated General Administration	6,272	1.0	1.0	1.4	5,707	.7	.8	1.1
	532,066	84.8	86.3	120.2	607,318	74.5	83.0	121.4
Premium Taxes & Licences	13,799	2.2	2.2	3.1	16,305	2.0	2.2	3.3
Profit/(Loss) Before Taxes & Investment Income	(67,526)	(10.8)	(10.9)	(15.3)	(62,462)	(7.7)	(8.5)	(12.5)
Investment Income								
Income	63,113	10.1	10.2	14.3	71,170	8.7	9.7	14.2
Direct Administration Cost	799	.1	.1	.2	969	.1	.1	.2
	62,314	10.0	10.1	14.1	70,201	8.6	9.6	14.0
Other Income/(Expense)	(776)	(.1)	(.1)	(.2)	(704)	(.1)	(.1)	(.1)
Profit/(Loss) Before Income Taxes	(5,988)	(.9)	(.9)	(1.4)	7,035	.8	1.0	1.4

APPENDIX L

(referred to in Chapter 13)

THE I.I.A.B.O. AGENCY STUDY*

Commission paid to agents represents about 14% of the total dollar value of commissions paid by the industry to the total dollar value of premiums earned from automobile insurance.

In order to examine the composition of this 14%, reference was made to the November, 1977 issue of *Canadian Insurance* which contained an abridged version of a recent Agency Study sponsored in part by the Independent Insurance Agents and Brokers of Ontario (I.I.A.B.O.). While this study included agencies in other Provinces, it has been taken as representative of Ontario (6 Ontario agencies were included) for want of better information. Fourteen sample agencies were included in the study and the agency profile was approximately as follows:

Premium Range	Number of Agencies	Agencies Distributed by Number of Insurance Company Contracts				
		1-5	6-10	11-15	16-20	21-25
Less than 500,000	1	—	1	—	—	—
\$ 500,001—1,000,000	5	1	1	3	—	—
\$1,000,000—1,500,000	5	1	2	1	—	1
\$1,500,001—2,000,000	3	—	1	2	—	—
Total Number	14	2	5	6	—	1

In Exhibit 1 below, the results of the “best average agency” are estimated using details provided in the article and the approximate profit from automobile insurance commissions has been calculated.

EXHIBIT 1
OPERATING COST STRUCTURE OF THE “BEST AVERAGE AGENCY”

	“Best Average Agency”	Lines of Business			
		Total	Personal	Commercial	Automobile
Premiums	100.0%	100.0%	20.0%	19.0%	61.0%
Commissions	16.4%	100.0%	30.0%	26.0%	44.0%
Expenses: Labour (65%)					24.7
All others (35%)					13.3
Total Expenses	13.7	83.5	26.0	19.5	38.0
Profit Before Taxes	2.7%	16.5%	4.0%	6.5%	6.0%

Source: *Canadian Insurance*, November 1977.

* Extract from Report X to the Committee from Woods, Gordon & Co., its consultants.

The Committee has considered the following facts from the article and conclusions which may be drawn from analysis of these facts:

1. "In 1965, the agency cost study produced figures of (commission income of) 18.2% of premium volume. By 1972, this had declined to 17.1% of premium and for our current study was 16.4%. As the financial statements analyzed only reflected a portion of the year in which commission reductions occurred, we anticipate this average will decline further in 1978."
2. Automobile insurance premiums represented approximately 61% of the total premiums and 44% of the gross commission income of the sample agencies.
3. "Of the 16.4% received, the best average agency retained 2.7% before the payment of income taxes. This amount, net of taxation, would be available for all the principals to share as return on investment".

This comment has several implications, namely:

- To the extent that they were active in the business, the principals' wages appear to have been included in the cost of labour.
 - A 2.7% retention on 16.4% in commission represents roughly a 16.5% return on commissions income, after principals' wages.
4. The "best average agency" earned roughly a 15% return on automobile commissions as demonstrated in Exhibit 2. In addition, it has been possible in Exhibit 2 to extend the analysis of commission income to the Ontario industry "average" experience of 14% on premiums earned. It should be recognized, however, that these estimations are based on the results of the "best average agency". Accordingly, these estimates have been adjusted downward for inefficiency factors in order to obtain order of magnitude estimates about the entire agency system. For illustrative purposes, it has been assumed that the average agency will retain only about one-half of the amount of the "best average agency", thereby earning a 7.5% return on auto insurance commissions.

EXHIBIT 2
ESTIMATED ELEMENTS OF COST/PROFIT IN
AUTOMOBILE LINES FOR THE ONTARIO AGENCY SYSTEM

	"Best Average Agency"*	Percent of Commission Income %	Ontario Agency System** (Average Agency)	Percent of Commission Income %
Commissions (Automobile)	44.0	100.0	14.0	100.0
Expenses Labour	24.7	55.0	7.7	55.0
All Other Expenses	13.3	30.0	4.2	30.0
Possible Inefficiencies	—	—	1.1	7.5
Total	38.0	85.0	13.0	92.5
Profit Before Taxes	6.0	15.0	1.0	7.5

* Percentage of Commissions Earned on all lines of Insurance.

** Percentage of Premiums Earned by the Automobile Insurance Industry.

BACKGROUND STUDIES

BACKGROUND STUDY ONE
Automobile Accident Compensation
The “No-Fault” Approach
TABLE OF CONTENTS

	Page
A. INTRODUCTION	265
1. The Common Law System of Liability	266
2. Compensation for Bodily Injury	267
3. Compensation for Vehicle and Property Damage	268
4. Benefits Paid by the Insurance Industry	268
B. A PURE NO-FAULT AUTOMOBILE INSURANCE SYSTEM: BASIC OBJECTIVES	269
1. Pure No-Fault Applied to Bodily Injury	269
2. Pure No-Fault Applied to Property Damage	269
C. ELIMINATING FAULT FROM COMPENSATION FOR BODILY INJURY	271
1. The Principle of Universal Compensation	272
2. The Difficulty of Proving Liability	272
3. The Inefficiency of Recovering from Third-Parties	274
4. The Objective to Penalize or Deter Negligent Behaviour	278
5. The Insurance Industry’s Attitude to Fault Determination	279
6. Reforms to the Fault System	280
7. Summary	282
D. COMPENSATION OBJECTIVES OF PURE NO-FAULT IN BODILY INJURY CASES	282
1. Security of Compensation	283
2. Efficiency Goals of Pure No-Fault	284
3. Periodic Payments	285
4. Non-Economic Loss	286
5. Methods of Assessing Compensation under Pure No-Fault ...	288
6. Summary	294
E. OTHER CONSIDERATIONS WITH REGARD TO NO-FAULT COVERAGE FOR MOTOR VEHICLE INJURIES	294
1. Judging the Performance of the Insurer	294
2. Awareness of the Limits of Coverage	295
3. Fraudulent Claims	295
4. Merit-Rating and Surcharges	295
5. Subrogation between Insurers and by Collateral Benefit Sources	296
6. Benefits for Non-Residents and Out-of-Province Coverage ...	297

7. Rating	297
8. Insurance Coverage	298
9. Breach of Condition	300
10. Appeal or Review Procedure under Pure No-Fault	301
11. Summary	302
 F. A COMPROMISE APPROACH: NO-FAULT WITHOUT ABANDONING THE FAULT CONCEPT	303
1. Major Issues in the Fault/No-Fault Debate	303
2. The Compromise Approach	307
3. Methods of Combining Fault and No-Fault	309
4. Advantages of a Mixed Fault/No-Fault Approach	311
5. Weaknesses of a Mixed Fault/No-Fault Approach	314
6. Summary	316
 G. THE COST CONSEQUENCES OF NO-FAULT	318
1. Cost of the Current Ontario System of Reparations for Automobile Accident Losses	319
2. Improvements in Cost Efficiency Under No-Fault	321
3. Redistribution of Total Benefit Costs Under a No-Fault System of Reparations	325
 H. INITIATIVES TOWARDS NO-FAULT IN ONTARIO AND IN OTHER JURISDICTIONS	336
1. No-Fault Developments in Ontario	337
2. No-Fault Developments Elsewhere in Canada	338
3. U.S. Initiatives Towards No-Fault	339
4. No-Fault in New Zealand, Australia and Great Britain	342
5. Features of Selected Automobile Insurance Plans and Proposals	343
 I. NO-FAULT INSURANCE FOR PROPERTY DAMAGE	349
1. Introduction	349
2. The Savings Objectives of No-Fault for Property Damage	350
3. Cost Redistribution and Choice of Coverage	353
4. Deductible Recovery	357
5. Abuse of No-Fault System	359
6. Coverage for Vehicle Damage in Other Jurisdictions	360
7. Property Other Than Vehicles and Contents	361
8. Overview	361

APPENDICES

Appendix A: Details of Selected Plans or Proposals for No-Fault Coverage

Appendix B: Motor Vehicle Claims in the Courts

Appendix C: Worksheets for Cost Calculations in Sections G and I

BACKGROUND STUDY ONE

Automobile Accident Compensation The No-Fault Approach

A. INTRODUCTION

In the course of its study of the automobile insurance industry, the Committee has received submissions and material describing various systems of no-fault automobile insurance that have been suggested for various jurisdictions in North America and elsewhere around the world. The Committee's examination of this topic has shown that "no-fault insurance" is a loose term that is used to cover a wide spectrum of automobile insurance schemes. Common to all these schemes is the right of the injured person to recover compensation without necessarily proving the existence of negligence on the part of the driver. Apart from this common concept, a broad variety of alternative proposals exist for no-fault recovery.

The following study is intended to clarify and define the no-fault approach to compensation, with reference to its possible ramifications in Ontario. This study organizes much of the material before the Committee regarding the fundamental concepts of no-fault automobile insurance. Accordingly it provides a detailed description of the concepts and features of:

- a) a *pure* no-fault system of automobile insurance;
- b) modified no-fault systems, incorporating some degree of recourse to tort action (third-party recovery on the basis of fault).

The various systems of no-fault compensation are outlined in this study under the following headings:

A. Introduction

The remainder of this section of the study provides a brief review of the current method of compensation in Ontario.

B. A Pure No-Fault Automobile Insurance System: Basic Objectives

A concise outline of a pure no-fault plan is presented here, together with commentary on the basic objectives of the no-fault approach to compensation.

C. Eliminating Fault from Compensation for Bodily Injury

In order to demonstrate why interest has grown in favour of totally eliminating fault as a basis for compensation, this section provides an outline of the principle of universal compensation and a review of the commonly mentioned shortcomings of the fault system.

D. Compensation Objectives of Pure No-Fault in Bodily Injury Cases

Adoption of the pure no-fault principle provides the opportunity for creation of an entirely new or revised compensation scheme for bodily injury. Over the last ten years, numerous proposals, varying widely in their method of calculating losses, have been developed under the no-fault label. This section outlines the objectives these proposals have in common and reviews common approaches towards assessment of the amount of compensation.

E. Other Considerations with Regard to No-Fault Coverage for Motor-Vehicle Injuries

This section presents further matters that must be considered in developing the eventual structure of a no-fault plan in order to ensure its effectiveness and fairness in providing compensation.

F. A Compromise Approach: No-Fault Without Abandoning the Fault Concept

Debate about the repercussions of a pure no-fault system and strong arguments on behalf of the tort system have created the need for a *compromise* solution to compensation that combines both fault and no-fault features. The general methods, advantages and weaknesses of the compromise solution are examined in this section.

G. The Cost Consequences of No-Fault

What are the cost consequences of no-fault? This section examines the two major elements that contribute to cost: inefficiency and total revenue required to support a given level of benefits. Consideration is given to three alternative approaches to no-fault: a pure no-fault system; a mixed fault/no-fault scheme; and a plan of enriched first-party benefits.

H. Initiatives Towards No-Fault in Ontario and in Other Jurisdictions

To provide a perspective concerning initiatives towards no-fault in Ontario and in other jurisdictions, this section first provides a brief history of no-fault development and, secondly, includes a detailed review of the categories of loss covered in a selection of alternative automobile insurance plans.

I. No-Fault Insurance for Property Damage

Consideration of no-fault related to property damage has been reserved for fuller discussion in this section. The objectives, the problems and the alternative methods of implementing a no-fault scheme for property damage are discussed.

As an introduction to the discussion on no-fault, a brief review of the current method of compensation in Ontario is presented below.

1. The Common Law System of Liability

The principal basis of compensation for automobile accident losses in Ontario is the common law system of liability. This system assigns the re-

sponsibility for payment of compensation to the party who's negligent conduct has caused an incident resulting in injury or damage. Otherwise stated, injured parties are entitled to receive complete recovery of damages, only if they can establish that their losses were caused by the negligence of another individual. Recovery of loss is reduced to the extent that a victim is at fault.

Compensation may be determined privately through negotiation between the victim and the negligent party or his insurer. Alternatively, the common law system of liability requires that a mechanism of courts and legal counsel be maintained to expedite recovery. The legal system serves the following functions:

- it ascertains whether there was negligent conduct directly causing injury;
- it obligates formally the negligent individual to pay damages;
- it calculates the amount of damages rightfully due the injured party.

In addition, it serves a secondary function—that of “punishing” negligent conduct by the imposition of liability. The obligation to pay damages is expected to act as a deterrent to careless driving, thereby reducing accidents and the need for compensation.

Operating in concert with the common law system of liability is the automobile insurance system. By purchasing third-party liability insurance, the negligent driver can take the loss, which he would normally be responsible to pay, and distribute it throughout the insured population of vehicle owners.

2. Compensation for Bodily Injury

To supplement compensation through the liability laws, Ontario has since 1972 required all vehicle owners purchasing liability insurance to protect others and themselves against their own personal loss from injury, by purchasing a standard level of Accident Benefits coverage. Compensation under this coverage is paid out without regard to fault.

In summary, the current automobile insurance system in Ontario distributes compensation for *bodily injury* under the following two categories:

- A. Basic benefits are paid regardless of fault to virtually *all* victims, on a first-party basis by the injured party's own insurer; or under the coverage of the vehicle owner if the injured party is a passenger or pedestrian. Benefits include *limited* payments for:
 - medical expenses
 - wage loss
 - funeral and death benefits
 - household replacement services.

B. Full recovery benefits are paid to *third parties* who are victims of negligence, to cover damages in excess of first-party benefits, under the same categories of:

- medical expenses
- wage loss
- funeral and death benefits
- household replacement services

and, in addition, payments are provided to compensate for:

- pain and suffering
- inconvenience, and
- other non-economic loss.

3. Compensation for Vehicle and Property Damage

Close to three-quarters of Ontario vehicle owners insure themselves against damage to or loss of their own vehicle, by purchasing collision, comprehensive, or specified perils coverage. Damages are paid by the policyholder's own insurer. However, the deductible portion can only be recovered through the liability system from the party at fault.

The liability system also entitles the driver, even if he is *not* insured against damage to his own car, to recovery of his losses in the event that the accident is not his fault. Similarly, an owner of other property who experiences losses through the carelessness of a driver is entitled to compensation under the fault system.

4. Benefits Paid by the Insurance Industry

In 1975, the insurance industry in Ontario paid out \$454 million in losses incurred as a result of automobile accidents involving insured private passenger vehicles. The distribution of benefits paid under different sections of the automobile policy is outlined below.

TABLE 1
BENEFITS PAID IN ACCIDENTS
INVOLVING PRIVATE PASSENGER VEHICLES
1975 Policy Year

	Benefits Paid \$ Million	Percent of Total
<i>Bodily Injury</i>		
Accident Benefits	\$ 25	6%
Third-Party Liability	156	34
	\$181	40%
<i>Property Damage</i>		
Vehicle Damage (First Party)	152	33
Third-Party Liability	121	27
	273	60
<i>Total Benefits Paid</i>	\$454	100%

Source: Insurance Bureau of Canada, 1976 *Automobile Insurance Experience*. (Green Book)

Benefits paid on a third-party basis under the liability system account for over 60% of losses paid by the insurance industry. Third-party payments to the innocent victim of an accident are most significant in the area of bodily injury: they account for 86% of the \$181 million paid to persons injured in automobile accidents.

First-party payments predominate in the area of property damage. 56% of the \$273 million in property damage losses is paid by insurers to their own policyholders.

B. A PURE NO-FAULT AUTOMOBILE INSURANCE SYSTEM: BASIC OBJECTIVES

1. Pure No-Fault Applied to Bodily Injury

A pure no-fault automobile insurance system covering *bodily injury* would require a law specifying the following:

- “An injured person would request compensation only from his or her own insurance company (first-party basis). He or she would *not be allowed to sue* anyone else for this purpose. Negligence, or fault, would be irrelevant.
- No-fault insurance would be compulsory, and all auto-insurers would be required to provide it, without the option of cancelling.
- The no-fault insurance would cover only economic losses due to injuries or fatalities—medical expenses, loss of income and expenses for substitute service.
- Since pain and suffering cannot be measured in dollars, these losses would not be covered.
- To minimize costs, duplicate payments for the same loss would be prohibited.”¹

In addition provision should also be made for the following factor:

- Compensation would be provided to all occupants of the vehicle, pedestrians and any person injured by the insured vehicle. Provision would also be made for compensation to persons injured by uninsured or unidentified vehicles.

A pure no-fault plan of automobile insurance as described above is foremost a compensation scheme. It proposes that the plight of automobile accident victims is a matter of social concern. The pure no-fault approach has two basic characteristics:

1. Elimination of Fault

It takes away the right of an injured party to sue a driver for recovery of losses, because it dispenses with the need for determining fault as

1. *Consumer Reports*, “Managing Your Auto Insurance”, August 1977, page 487.

a means for entitlement to compensation. Instead, it proposes to protect *all* automobile accident victims.

2. *Reform to the Compensation System*

It proposes to establish an efficient system of evaluating and paying damages, based on consistent and objective standards, that will protect all victims equally.

In comparison to a third-party or tort system of recovery, pure no-fault is intended to have the following benefits: it should reduce the amount of time required for processing claims and receiving benefits; it should be more equitable than the tort system by allocating benefits on the basis of defined losses; and a no-fault system should cost less to operate than a tort system. These benefits are achieved by eliminating the right to sue and substituting in its place recovery from the injured party's own insurer.

The no-fault principle goes one step further than the first-party approach to insurance. Under a *first-party approach*, each insurer takes on responsibility for the personal injury and property damage claims of its own policyholders but may be entitled to reimbursement of the amounts paid from the insurer of the party at fault. A *no-fault system* of compensation ensures that the first-party approach is extended to *all* claims, *and* it requires the alteration of legal relationships, namely the denial of the right of an injured party or his insurer to sue a driver for recovery of losses.

Under a no-fault system of automobile insurance a driver is responsible both for his own losses *and* under most no-fault plans for the losses incurred by *any* other person, as a result of an accident involving his vehicle. The no-fault principle gives a driver immunity from liability; in return, he must accept responsibility for the losses sustained by pedestrians and by occupants of his vehicle, by purchasing first-party insurance. In addition, first-party insurance allows him to protect himself and his family in the event of his own injury or in the event of damage to his own vehicle.

2. **Pure No-Fault Applied to Property Damage**

Under a no-fault approach applied to *vehicle or property damage*, responsibility for payment of losses would no longer be shifted to the driver at fault. If the vehicle owner is not insured against damage, he cannot sue anyone else for recovery and therefore must bear his own loss.

In order to safeguard owners of property other than vehicles and their contents, a no-fault approach also requires that every vehicle owner assume responsibility for damage to other property caused by his automobile, regardless of fault.

The objectives of a pure no-fault plan of insurance for property damage differ in emphasis from the objectives of a no-fault plan for bodily injury.

mainly because the need for recovery is more of individual than social concern. In addition, evaluation of the extent of damages is relatively straightforward and is the same under either the fault or no-fault systems.

The focus of no-fault property damage insurance is directed towards the reduction of costs and time spent in processing vehicle damage claims, by elimination of the right to sue and the need to determine fault. Both the insured and the public are expected to benefit—lower premiums for the insured, and savings to the public by taking vehicle damage suits out of the lower courts.

Section I at the end of this study will return to a more detailed discussion of alternatives and concerns in no-fault vehicle and property damage proposals. The remainder of this study will concentrate on the bodily injury aspects of pure no-fault proposals.

It is necessary to stress that the postponement to a later section of the discussion of no-fault as applied to vehicle damage, is not meant to suggest that the consideration of no-fault might be restricted to bodily injury only. Important benefits are to be achieved by incorporating property damage into the no-fault system. At the same time, serious harm can be done to the concept of no-fault in general, if the inclusion of property damage within a no-fault plan is not carried out with sufficient attention to the structuring of a workable system.

C. ELIMINATING FAULT FROM COMPENSATION FOR BODILY INJURY

Automobile accidents have been described as an "epidemic". In the manner of doctors faced with an epidemic, lawyers and traffic experts are exhorted to study the host (the automobile), the agent (the driver) and the environment before a meaningful attack can be made on the problem of accidents.¹

The fault system focuses primarily on the driver (the agent) as the cause of accidents: it states or implies that accidents are caused simply by carelessness and can be avoided if the driver will only be more cautious. Furthermore, fault applied to the system of compensation focuses chiefly on the suffering of one class of victim—the *innocent* victim.

As a contrast to the fault system, this section will first provide a brief review of the principle of universal compensation. It will then examine many of the commonly mentioned shortcomings of the fault system as a method of alleviating the personal and property losses created by the automobile accident epidemic. The purpose of this review is to demonstrate why

1. J. E. Gordon, "The Epidemiology of Accidents", in A. Linden, "The Prevention of Traffic Accidents", *Chitty's Law Journal*, No. 80, 1967.

interest has grown in favour of eliminating fault as the basis for entitlement to compensation for motor vehicle injuries.

1. The Principle of Universal Compensation

Any person injured in an automobile accident can expect to be compensated, to some degree, under the system of compensation known as "*pure no-fault*". As with public medical and health insurance in Ontario, every resident is assured that he will not be forced to bear his loss solely on his own.

In contrast to most current systems of automobile reparations which rest largely on the fault concept of shifting losses to the party to blame for an automobile accident, the universal system of compensation is labeled "*no-fault*". This label appears to have negative implications since it means the denial of the current fault system with all its advantages as well as disadvantages. However, the no-fault system is not strictly opposed to assigning blame, but rather in favour of guaranteeing to each victim the certainty that his losses will be met. This latter concern outweighs the first, and results in the basic premise of the pure no-fault approach—that negligence has no bearing on the need for compensation resulting from injury or fatality in a motor vehicle accident.

The no-fault approach, pure or modified, cannot be accepted unless there is agreement that the careless driver who crosses the centre line needs to be compensated as well as the careful driver he hits. The pure no-fault approach goes even further—it specifies that the careless driver will get the same recovery as the careful driver. It completely eliminates discrimination in compensation on the basis of fault.

The no-fault approach totally disclaims the loss shifting aspect of the negligence system. Loss-shifting means that responsibility for losses resulting from an accident is assigned to the person who caused them. Under the negligence system, a driver buys insurance so that he will not pay damages out of his own pocket if he carelessly causes an accident. His insurance entitles him to distribute his responsibility by going to a pool of funds from which he (or his insurer) can compensate the injured party.

Under the no-fault system, society as a whole is deemed responsible for motor vehicle injuries, by its dependence on use of the automobile. A driver therefore buys insurance because it is his community responsibility to contribute to a pool of funds to be made available to all victims of automobile accidents. Loss-sharing is emphasized under the no-fault approach, rather than loss-distribution which is necessary under the negligence system.

Leaving aside the basic no-fault premise that fault should be eliminated from compensation for bodily injury, the remainder of this section reviews the arguments commonly raised against the fault system in the way it carries out its more narrowly defined aim of compensating the innocent.

2. The Difficulty of Proving Liability

The chief priority of the fault liability system of compensation is to protect the *innocent* victim of negligence. It can be demonstrated by numerous examples that the fault system is an apparently complete method of compensation, protecting those injured persons who are fortunate enough to be successful in satisfying the legal tests of eligibility for full compensation.

However, it can also be demonstrated that this method of protecting the innocent victim has shortcomings associated with the need to *prove* negligence. To qualify for compensation, the supposedly innocent victim must first show that the conduct of another individual was the cause of the incident that gave rise to his injury. In the majority of cases, proof of liability is easily established.

But a number of factors can complicate proof of liability and exclude some victims from full recovery. Examples based on Ontario experience follow.

- a) Entitlement to full recovery is reduced in the event of shared liability, by the extent to which the claimant's conduct contributed to the incident causing injury. There is no evidence available to indicate how significant this exclusion is in Ontario. But it is important to note that the apportionment of fault makes the process of deciding claims more complicated. There is no scientific method to the division of fault and results can be quite arbitrary. It is for this reason that many of the states in the U.S.A. have hesitated to introduce "comparative" negligence laws that permit the fractioning of fault.
- b) Proof of liability in Ontario can be limited by certain statutory restrictions, for example:
 - The requirement to prove "gross negligence" in third-party claims involving passengers. Elimination of this restriction was recommended in the Committee's First Report on Automobile Insurance. Later, in November 1977, an amendment to the Highway Traffic Act removed the concept of "gross" negligence from the Ontario Law.
 - Defendants are able to argue "inevitable" accident and hence disprove liability. Changes in this restriction were considered in the First Report on Automobile Insurance, but a proposal to eliminate this concept was rejected until a more thorough consideration could be given to the general concept of no-fault.
- c) Eligibility for third-party compensation can be reduced by the complexity of proving liability. A number of factors confound proof of liability:
 - insufficient evidence or unreliability of witnesses;
 - delay in start of investigative procedures, making reconstruction of events unreliable;

- delay in bringing disputes to court, dimming recollection of events;
- speed and traffic congestion, confusing the sequence of events leading to the accident.

The Select Committee in its First Report on Automobile Insurance has already acknowledged "that there has been a vast change in the speed with which things happen" and therefore:

"the speed and complexity of modern driving conditions often make it a meaningless exercise to assess fault or blameworthiness among the participants in an accident".¹

Concern arises especially over the claims which go to court. Although the proportion is small, under 10%, some 20,000 lawsuits (including property damage) are started each year in Ontario and over 2,000 motor-vehicle cases are tried. (See Appendix B for summary data.) Delays of three to nine months are common in setting trial dates. If liability is contentious in any of these cases, delay is likely to obscure further the series of events leading up to the accident. The problem of delay is discussed further below.

- d) There is no entitlement to recovery under liability laws for the driver in a single-car accident, as there is usually no other person to blame for the injury. In 1976, 25% of persons injured in accidents in Ontario were involved in single-car collisions.² In most cases the injured drivers in single-car collisions were ineligible for recovery through the liability system. It is sometimes argued that this is no indictment of the tort liability system, as it was never intended to compensate the careless, drunken or suicidal driver; but not all single-car accidents are caused by negligent behaviour.

3. The Inefficiency of Recovering from Third Parties

Three major factors make a system of recovery from a third party on the basis of fault inefficient:

- Delay in recovery;
- High cost of recovery; and
- Inability to recover from the negligent party.

These factors and their significance in Ontario are discussed below.

Delay in Recovery

The negligence system of recovery can be cumbersome and slow for those claims that go through the full process of recovery. This means that

1. Select Committee on Company Law, *The Insurance Industry—First Report on Automobile Insurance*, Province of Ontario Legislative Assembly, 1977, page 66.
 2. Ontario Ministry of Transportation and Communications, "Motor Vehicle Accident Facts", 1976.

the victim's entitlement may not be immediately predictable, nor promptly paid. Uncertainty and delay can hinder physical recovery, increase inconvenience, set back rehabilitation, and prolong a feeling of grievance. Delay is costly to the insurer as well. Claims handling and legal expenses increase with delay, and these costs are passed onto the premium-paying public.

Delay is inherent in a system of recovery from third parties because an adversary situation is created that includes numerous procedures such as:

- a fault investigative process;
- a claim assessment process;
- a dispute settling process, in or out of court.

For these procedures to function effectively, it is often necessary to incur delay. As an example, delay in start of legal proceedings may be necessary to extend the time limitation for court recovery, in order to allow for full assessment of the extent of bodily injury.

Delays can also result from factors not related to the fault system. For example, differences in methods of handling claims among various insurers cause delays in some settlements.

There is unfortunately little current empirical evidence to describe the length or nature of delays in compensating motor vehicle accident victims in Ontario under the present system of settling third-party claims. A study conducted across Canada, excluding Ontario, showed that in 1971 over 50% of motor vehicle civil actions took more than one year to settle.¹ Studies carried out in the Province of Quebec² and in the United States³ point out that the length of time to settle a claim increases in proportion to the amount of compensation.

Based on development of claims in previous years, the Insurance Bureau of Canada indicates that, in recent experience in Canada, 54% of third-party claims over \$50,000 are settled in the first year, 24% during the second year, and the remaining 22% in the third year or later. 1976 Green Book data show that for all claims combined, 23% of the *amount* of claims incurred in a given policy year is still outstanding 3 years later, and 13% is still outstanding 4 years later, although only 1-2% of the total *number* of claims are involved in such delay.

Payment of interest from the date of accident or start of court action is one method of alleviating the problem of delay. In November 1977, the Judicature Act in Ontario was amended to require payment of prejudgement interest, at the prime rate, from the date the action commenced to the date of

1. See Appendix B for reference and summary data on motor vehicle claims before the courts.

2. Government of Quebec, *Report of the Committee of Inquiry on Automobile Insurance*, March 1974.

3. U.S. Department of Transportation, *Motor Vehicle Crash Losses and Their Compensation in the United States*, March 1971.

judgement. The judge may fix a rate of interest higher or lower than the prime rate.* Certain difficulties however remain:

- The claimant can still suffer from financial problems prior to claims settlement, and possibly incur debt at a higher rate than the interest on his award.
- Payment of interest may encourage greater delay, as the chance for higher settlement is made less risky by interest paid.
- Nominal interest rates may encourage insurance companies to prolong settlement or appeal claims in order to reach lower settlements.
- Delay is often the responsibility of the claimant or lawyer who fails to institute court action within an expeditious period of time. However, the burden of payment for an interest penalty dating from the time of the accident is borne by the insuring public.

The pure no-fault approach eliminates delay directly related to the fault investigative process and, by substituting a direct relationship between victim and insurer, it can also reduce delay in the claims assessment process. Of course, time is also necessary to process two-party claims, as expenses must be verified and the economic status of the disabled person must be examined. But, payment is intended to begin as soon as verification of injury or disability is received and evaluated. Disagreement over the amount of compensation can be settled without affecting the start of at least partial compensation.

High Cost of Recovery

Extensive claim settling costs can be accumulated in a third-party system of recovery. Both the claimant and the insurer bear some portion of these expenses. To function effectively, the fault system requires that experts be employed to collect evidence, assess the value of this evidence, negotiate with the other side, and sometimes present a case in court.

The injured victim is most affected by the legal costs associated with exercising his full rights under the fault/liability system. Experience in Quebec¹ and British Columbia² prior to government ownership indicated that an average of 20% to 30% of bodily injury claims resulted in legal advice being sought by the injured party.

Not all these costs can be recovered by the innocent victim. The injured party undertaking legal proceedings takes a gamble that his claim will succeed, and in Ontario is charged with his own costs, and sometimes those of the third party, if his claim is turned down in court. Even the successful

* *An act to amend The Judicature Act*, Province of Ontario, November 8, 1977, Section 3.

1. Government of Quebec, *Report of the Committee of Inquiry on Automobile Insurance*, March 1974, Table 4, page 197.

2. Province of British Columbia, *Royal Commission on Automobile Insurance*, 1968, Table 2.1, page 99, Volume 1.

claimant may find that the amount added onto his award to cover legal fees is less than his actual expenses. As an example, a judgement of contributory negligence will reduce the settlement amount paid to an injured person, including the portion for legal fees, but the claimant's actual expenses are not reduced.

Again, data to segregate the costs of the third-party system of recovery are difficult to develop in Ontario. For example, legal expenses and claims adjusting costs are not segregated by the insurance industry in their reporting of losses incurred in the Province. However, insurance companies state that it is a rule of thumb in the industry that in claims settled by the insurance company's adjusters, legal costs of the injured party amount to about 15% of the award amount. These fees, additional costs borne by both successful and unsuccessful claimants, and internal legal expenses of insurance companies are largely eliminated under a pure no-fault insurance system.

Estimates of legal costs are developed later in Section G of this study.

Inability to Recover from the Negligent Party

Recovery under the tort liability system is also limited by the ability of the responsible party to pay. At present, every third party who is first able to prove liability can receive compensation up to \$100,000: either from the \$100,000 minimum liability insurance carried by the approximately 90% of drivers in Ontario who are insured; or from the Motor Vehicle Accident Claims Fund when the negligent driver is not insured or cannot be identified.

Data developed by the Insurance Bureau of Canada indicate that the \$100,000 limit is sufficient currently to cover over 99% of personal injury claims brought to private insurers in Canada for payment.

However, individual cases are important when serious or permanent injury is involved. I.B.C. data show that 40 percent of drivers in 1977 were insured only up to the minimum coverage limits of \$100,000. For those persons whose losses could exceed \$100,000, chances are a little better than even that the negligent party has sufficient insurance coverage to compensate them fully for serious injuries. It should be noted, however, that policy limits have been generally increasing: in 1971 only 24% of insureds carried coverage of over \$200,000 inclusive, compared to 46% in early 1977.

In its First Report on Automobile Insurance, the Select Committee on Company Law proposed that limits for liability coverage be made an *unlimited* amount.¹ Along with the Committee's recommendation for *compulsory* insurance,² unlimited liability coverage would eliminate a potentially serious flaw of the negligence system of compensation.

1. The Select Committee on Company Law, *First Report on Automobile Insurance*, page 58.

2. *Ibid.*, page 173.

The alternate means of guaranteeing full recovery is compulsory no-fault insurance. This method goes further than extension of liability limits under a compulsory insurance system: unlimited liability limits protect only the *innocent* victim against a shortfall in recovery; compulsory no-fault is intended to protect *all* victims.

At the same time, it is important to note that the no-fault system may define the extent of loss in a different manner than the fault system, so the amount of recovery by the innocent victim may be less than under the fault system. This subject is discussed further in Section D.

4. The Objective to Penalize or Deter Negligent Conduct

A recurring argument in favour of the fault/liability system and against a no-fault system states that the fault system is moral and promotes individual responsibility, while the no-fault system is immoral in treating innocent and guilty alike and in diluting individual responsibility.

Numerous arguments have been advanced both for and against the "punitive" and "deterrent" values of the fault system. The fault system claims that:

- Subjection of the negligent driver to court proceedings and formal declaration that he is responsible for an accident will have a deterrent impact on all drivers.
- Denial of compensation to the negligent driver will encourage responsibility for one's conduct, as the negligent driver must absorb his own losses.

In addition, the fault system claims that punishment of the guilty through a court process will serve a psychological function by solacing the innocent. Pure no-fault denies the victim, who feels wronged, the ability to fight for his rights in a court of law.

On the side opposed to the fault system is the conclusion of the 1971 U.S. Department of Transportation study on *Automobile Accident Compensation* which states:

"... that most accidents are caused by environmental or personal factors which are external to the individual's conscious control and that punishment or its threat, therefore, is ineffective as a deterrent to deviant driving behaviour."¹

In addition, it is commonly argued that there is no deterrence value to the tort system when 90% or so of Ontario drivers are aware that any damages they cause will be paid for by their insurer. Nor will the guilty driver's

1. U.S. Department of Transportation, *Motor Vehicle Crash Losses and Their Compensation in the United States*, report by John A. Volpe, Secretary of Transportation, March 1971.

premium reflect the degree of his fault. It may reflect the fact that he had been in an accident, but the amount of loss caused by his negligence is reflected only in the total loss statistics of the class into which he happens to fall.

The fault principle has also been challenged from a theoretical viewpoint. A background report to the 1977 Manitoba White Paper on *Sickness and Accident Compensation*¹ states that, if ethical retribution is the aim of the fault principle, damages should be assessed in relation to the degree of negligence: the more reprehensible the conduct, the more a driver should pay. But the quantum of damages under tort law is treated quite independently from a consideration of the defendant's conduct. A lapse of attention can result in serious injury and impose a heavy burden of responsibility on the driver "at fault".

Secondly, if the fault principle holds a defendant *morally* to blame for an accident, then there should be a subjective examination of the defendant's own state of mind to determine whether he personally appreciated that his conduct posed a danger to others, but went ahead with it regardless. Instead, conduct is judged by the objective standard of the elusive "reasonable man".

In contrast, the pure no-fault system denies the principle of retribution that says the wrongdoer should bear the burden of losses caused by his conduct. Furthermore, pure no-fault proposals make no effort to penalize or deter negligent conduct. Deterrence is left to criminal law, or ultimately to the individual who is faced with the prospect of his own death or severe injury as a result of careless driving.

5. The Insurance Industry's Attitude to Fault Determination

In response to widespread interest in the no-fault theme, and initiatives in many jurisdictions, the insurance industry in Canada prepared in 1974 its own "no-fault" plan of automobile insurance called Variplan—Vehicle Accident Recovery Insurance Plan. The Insurance Bureau of Canada, who sponsored development of Variplan, has indicated before the Committee² that a major aim of this plan is to achieve both time and dollar savings in compensating accident victims by restricting the need for fault determination in all but serious injury cases.

Insurance companies in Ontario have already cooperated amongst themselves to reduce the costs and vexation of fault determination. For example, Ontario insurers already subscribe to the "knock-for-knock" princi-

1. Government of Manitoba, White Paper on *Accident and Sickness Compensation in Manitoba*, "The Negligence Action: A Discussion Paper", Volume Two, May 1977.
2. Proceedings of the Select Committee on Company Law, Remarks by Mr. C. Fraser on behalf of the Insurance Bureau of Canada, August 18, 1977.

ple. This means they are willing to deal with their own policyholders in paying out certain claims without regard to fault, since the companies as a whole insure the total market and their own policyholder losses tend to level out to the market average in the long-run.

Insurance companies apply the knock-for-knock principle in waiving the right to subrogation against other companies for first-party Accident Benefits payments, and they apply it in the property damage area by using the "collision assessment chart", or "intercompany settlement chart", whereby fault is apportioned in certain common accident situations according to diagrammatic charts, rather than by means of a thorough fault investigation. Any rough justice in individual settlements averages out for the insurance companies under the knock-for-knock principle.

In addition, the complexity of proving liability has caused insurance companies in Ontario to adopt an ad hoc "sharing of liability" approach in at least one case:

For example, in a 32-vehicle pile-up on Highway 400 south of Barrie, in March 1973, twelve people were killed and 40 others injured. Defendants in this case decided early on that it would be difficult to sort out who was liable in view of the number of vehicles involved. Three years later they agreed to set up a liability fund to which each insurance company would contribute an equal amount regardless of liability. Each insurance company also agreed to absorb its own collision and property damage costs regardless of fault.¹

This shared liability approach permitted the majority of persons injured in this accident to recover damages. If negligence or contributory negligence had been assigned to particular individuals, they would not have been able to recover under the third-party liability system. Compensation of the "innocent" may well have been limited also, as the total amount of funds available for compensation would have been restricted by the liability coverage of the "guilty".

6. Reforms to the Fault System

A variety of reforms to the fault system as it operates in Ontario today have been suggested, some dating from the early 1960's. These reform proposals are intended to improve the third-party system of compensation, extending compensation to more victims and reducing delays. They should be considered in the context that the victim in Ontario is already in a situation where he does not have to rely entirely on the fault system, as Accident Benefits coverage provides some compensation to nearly all injured persons. Nevertheless, if the primary objective of a scheme of compensation is the availability of a satisfactory level of indemnity to all victims regardless of fault, then these reforms fall short of this objective.

1. *Globe and Mail*, "10 will share \$297,500 in settlement of 1973 Barrie crash", December 23, 1976.

Several of the following reform proposals have been discussed. Aside from expansion of no-fault benefits under Accident Benefits coverage, reforms to the fault/liability system could include.¹

- The liability limits on the automobile policy should be unlimited.
- Liability insurance should be compulsory, and an effective means of assigning risks should be provided to cover motorists unable to insure themselves through normal channels.
- More use of the advance payment under Section 223 of the Insurance Act should be made.
- In a dispute between two insurers over who is obligated to pay Accident Benefits, legislation should provide that the two insurers pay the victim on an equal basis and let the issue between them be determined at a later date.
- More stringent rules are required to speed up the judicial process; for example, ruling a claim or an appeal to be deemed abandoned unless pleadings are delivered and actions are set down within a certain period of time. The Government of Ontario announced in February 1978 its intention to improve a number of the aspects of the judicial system; specific proposals were not announced.
- Pre-trial proceedings should be given greater emphasis, requiring counsel to review liability aspects early on and to appraise the nature and extent of damages well before trial.
- The defence of inevitable or unavoidable accident based upon a mechanical defect should be eliminated. The owner of a car should be subject to absolute liability for the mechanical condition of his vehicle.
- Overutilization of tort recovery can be controlled by advising the jury of first-party benefits available; by requiring two verdicts, one for residual special damages and one for general damages; and by amending the criminal code to treat insurance fraud as a serious crime.

In many cases reforms such as those suggested above expand the fault system to include as many victims as possible within the liability system of recovery. For example, in order to allow the gratuitous passenger to recover damages from his host driver under the guest passenger provision of the Highway Traffic Act, the trend had been for courts to rule "gross negligence" even when there was no conscious wrong-doing by the driver. This practice permitted the passenger to recover his losses, but placed a charge of gross negligence on the driver who may have departed unconsciously from "the standards by which responsible and competent people in charge of motor cars habitually govern themselves".² Amendments to the Highway Traffic Act in November 1977 have since removed the concept of "gross" negligence from the Ontario law respecting automobile accidents.

1. Several of the suggested reforms are taken from: *Submission of the Insurance Committee of the Advocate's Society with respect to No-Fault Automobile Insurance*, February 4, 1975.

2. *Flavin vs. Duggan*, Supreme Court of Nova Scotia, March 30, 1977, reported in Reardon, J.D., Q.C., "The guest passenger and gross negligence", *Canadian Underwriter*, August 1977.

7. Summary

The main issue in the foregoing comparison of the fault and no-fault approaches to compensation can be summarized into one basic question: Should fault determination have *ANY* bearing on compensation? In addressing this issue consideration should be given to two factors.

- Is it morally acceptable to the public to disregard wrongful action when considering entitlement to compensation? Would the public be satisfied with a compensation system that provides indemnity to the guilty driver as well as the innocent victim, eliminates the concept of retribution, and leaves punishment for negligence entirely to the criminal division of the courts?
- Is there some practical reason for discrimination in compensation? For example, is discrimination on the basis of fault necessary as a method of containing and allocating the costs of compensation? If so, should compensation be provided foremost to innocent victims, on a full recovery basis?

It is possible to answer yes to both the above questions—hence the dilemma inherent in the fault/no-fault debate. The practical aspects of a pure no-fault method of compensation can be independent of the acceptability of the pure no-fault principle. Therefore, it is possible to make the moral judgement that all persons should be entitled to compensation *and*, at the same time, to arrive at the conclusion that the fault system serves a practical purpose: it discriminates against the wrongdoer by denying him full recovery and thus keeps the costs of compensation at a level lower than under universal compensation.

To aid in answering the second question posed above, alternatives to the pure no-fault and pure fault systems, and their practical and financial aspects, will be described in Sections F and G of this study.

With respect to the first question above, reference is sometimes made to public opinion surveys in order to derive a true and reliable answer. However, public opinion polls conducted in other jurisdictions have generally produced contradictory results. Many respondents have declared themselves to be uninformed or undecided when asked about a no-fault approach to automobile insurance. Many have judged no-fault on its application to property damage settlements and have indicated disapproval of the concept. Public misunderstanding of the no-fault issue has prompted legislators in a number of jurisdictions to initiate without public survey the move to no-fault coverage for bodily injury.

D. COMPENSATION OBJECTIVES OF PURE NO-FAULT IN BODILY INJURY CASES

Any system of compensation which provides some measure of indemnity to *every* person injured as a result of an automobile accident, *and* does

not provide any additional compensation based on blame for the accident, potentially falls within the category of a *pure* no-fault system.

As a result, numerous proposals, varying widely in their method of calculating losses and the amount of indemnity, have been developed over the last ten years based on the no-fault principle. The majority of proposals have these common objectives:

1. To compensate *all* victims and to spread costs across the entire driving community.
2. To compensate efficiently.
3. To compensate on the basis of consistent and objective standards.
4. To stress actual expenses and earnings-related compensation in evaluating losses.

This section examines in more detail how a pure no-fault plan attempts to meet these objectives, and outlines common approaches towards assessment of the amount of compensation to be provided.

1. Security of Compensation

Since a pure no-fault system proposed to compensate all victims of motor vehicle accidents, it must provide security in compensation.

This goal can only be achieved if coverage is universal; that is, a pure no-fault insurance plan must be *compulsory*. Compulsory coverage invokes the principle of reciprocal benefit and obligation, advocated by the Committee in its First Report, namely:

“that every person who owns an automobile that is used on public roads has a moral obligation—and ought to have a corresponding legal obligation—to bear his fair share of the losses that are incurred on the roads and should be entitled to benefit from the payment by other automobile operators of *their* fair share of such losses through *their* insurance premiums.”¹

The pure no-fault approach to insurance incorporates this principle of universal obligation and it also provides a mechanism by which the reciprocal entitlement to benefits can be shared by all (without regard to fault), thereby providing security for all.

A further aim of no-fault is to guarantee that as soon as anyone has suffered injury, he should know whether or not he will be compensated. Therefore, the no-fault system *pre-defines the nature and amount of compensation* available and assigns responsibility for payment to the injured party's own insurer.

1. The Select Committee on Company Law, *First Report on Automobile Insurance*, page 173.

2. Efficiency Goals of Pure No-Fault

Pure no-fault proposes to compensate all victims equally and to spread these losses across the entire driving community. Because full community participation is required, pure no-fault has the obligation to be efficient, as well as equitable.

To be efficient, pure no-fault must satisfy some of the following criteria:

- It must provide *prompt* compensation. Prompt compensation reduces uncertainty, frees the injured party from financial problems, and encourages rehabilitation.
- It must provide a *simple* and objective procedure of recovery that is well understood by the public. Simplified procedures will speed payment of compensation and will reduce costs of processing in contrast to a system which considers each case to be "exceptional".
- It must be *flexible*. It must provide a process of revising indemnities to meet changing circumstances in the cost of living, in the concerns of society, and in the needs of the injured person.
- It must attempt to *eliminate duplicate payments* for the same loss. A pure no-fault system intends that all damage costs related to "normal" use of the automobile be accounted for and spread across the entire driving community.

Therefore, pure no-fault proposes that *automobile insurance be the first payor* of indemnities for motor vehicle injuries, and that duplicate payments be avoided. Eliminating duplicate payments frees resources in the community for better uses, and lowers total disability insurance costs to the public. Auto insurance as first payor eliminates the problem for the auto insurer of integrating indemnities or of integrating premiums under various disability policies. Accordingly, other benefit plans would be required to adjust their policies to exclude coverage for motor vehicle injuries.

For those situations in which publically supported insurance schemes apply, which provide essential or universal benefits, auto insurance as first payor may be impractical or may create delays in delivery of services. In addition, repayment through subrogation of the costs incurred by these schemes is inconsistent with a uniform system of no third-party recovery. As a result, benefits received from these schemes should either be subtracted from no-fault automobile insurance coverage, or reimbursed by the auto insurer on some pro-rata no-fault basis.

- It must *minimize expenses* of administration and claims settlement. A primary goal of pure no-fault is to return more of the premium dollar to the injured person. Although no-fault eliminates some of the costs of

dealing with third parties, it does not automatically lead to improved claims handling procedures or administrative methods.

Reduced administrative and claims costs are a goal of both the no-fault and the liability insurance systems, and are discussed in other areas of the Committee's study of automobile insurance. An illustration of how pure no-fault can reduce costs by eliminating the function of dealing with third parties is presented in Section G.

3. Periodic Payments

A pure no-fault system rejects a single and final assessment of damages as an appropriate method of compensation for most categories of loss. Many of the goals of pure no-fault, such as security and promptness of payment, are not met by a point-in-time assessment.

In contrast, as it is currently structured, the third-party liability system evaluates compensation at a given point in time to cover both economic and non-economic loss, both in the past and in the future. This assessment is final and results in a lump-sum payment.

There are several reasons why the point-in-time method of assessment is used by the liability system of compensation:

- Legal tradition states that payment must include compensation for all losses incurred as a result of negligence, and that a claimant has the right to demand *full* payment.
- Payment is final and discharges the negligent party and his insurer from on-going responsibility.
- With a fixed-sum award, the claimant can compare his award against the limits of the negligent party's liability coverage, to determine whether or not he will be able to recover fully.
- A closed settlement reduces uncertainty for insurers in predicting their claim reserves, by establishing limits to loss payout and allowing the majority of files to be closed within predictable periods of time.

However, valid reasons also exist to dispute the appropriateness of the single, fixed-sum payment of damages:

1. It is impossible to predict accurately at a point in time future loss of earnings, future medical condition, or future life contingencies. Therefore, fixed-sum payments are likely to either undercompensate or overcompensate.
2. It is impossible to adjust a lump-sum award to changes in circumstances or medical condition. Therefore, there is an incentive to delay the date of assessment until as much evidence as possible has been accumulated to support a claim.

3. The claimant receiving a fixed-sum award may use his award in whatever way he wishes, possibly in an unwise manner—for example, by spending it quickly rather than investing it or purchasing an annuity to replace his loss of regular income.
4. A fixed-sum award, calculated to represent a lifetime of benefits, can be a “windfall” gain to the injured person’s estate in the event of his early death.

These disadvantages have been the main reasons why a no-fault system takes a periodic payment approach to compensation. Periodic payments allow the no-fault system to meet losses as they arise. Losses can be assessed and paid without delay, and can be adjusted at a later date, if necessary.

The Insurance Bureau of Canada, in its response to the First Report of the Select Committee¹, has suggested that consideration be given, within the context of the tort system, to the provision of annuities for those who are seriously or permanently disabled. It suggests that the insurer be required to establish a capital fund from which such annuities would be payable and that this fund would revert to the insurance pool upon the death of the injured party.

However, given the tort requirement for final awards, the capital sum awarded in damages is not subject to adjustment in the event of changes in medical condition or other life contingencies. An annuity approach to indemnity under the tort system resolves the problem of matching payments to life expectancy, but the rigidity of tort in assigning final awards does not permit adjustment of the total value of the annuity to changes in the injured party’s circumstances. This process of review can be built into a pure no-fault system.

4. Non-Economic Loss

A pure no-fault system proposes to compensate all victims on the basis of consistent and objective standards. In contrast, the negligence system of compensation was accused by the Saskatchewan Reparations Committee of indemnifying some persons more for the same injuries than others:

“There is no rule in Canada that requires uniformity or consistency of amounts as between claimants. This means that the subjective values of judge or jury, their cultural backgrounds and their experience and financial management and other economic affairs, coupled with the skill of legal counsel, result in a wide variation of awards.”²

1. Insurance Bureau of Canada, “Submission in Response to the First Report of the Select Committee on Company Law”, October 1977, page 18.

2. The Saskatchewan Government Insurance Office, *Reparations for Motor Vehicle Accidents*. A Brief to the Ministers Advisory Committee on Reparations for Motor Vehicle Accidents, October 13, 1976.

The above criticism is directed primarily at awards for *non-economic loss*, which are widely criticized on a number of factors. For example, payments for non-economic loss are considered to be inequitable because they encourage overcompensation for small losses. Insurers tend to be generous in small general damage claims to keep legal costs low and cases out of court. R. E. Keeton and J. O. O'Connell in the U.S. found that insurers pay for pain and suffering, just to avoid their own "pain and suffering" in seeing a claim file through court.

Other arguments have been put forward stating that the current auto reparations system sometimes encourages fraud, or at least exaggeration, among injured parties in order to qualify for pain and suffering awards as a "fringe benefit" of insurance compensation.

There is also the contention that recent large payments for non-economic loss are making some victims unreasonably wealthy. One case recently before the Supreme Court of Canada involved a young girl who was struck by a car in 1969 at the age of five. Doctors say this girl will never be able to work, marry or look after herself because she cannot control her arms, and walks and speaks with great difficulty. She was awarded \$950,000, later reduced to \$875,000 by the Ontario Supreme Court. \$200,000 of the award was allowed for pain and suffering. The driver of the car fought the size of the award, which, if well invested, would make the girl wealthy "far beyond any reasonable expectation that she would have had should she not have been injured". The Supreme Court of Canada was asked in this and two other appeal cases to establish some clear principles that would help lower courts to decide "what price to put on a broken body".¹

In its judgement in January 1978 concerning the case of the young girl, the Supreme Court further reduced the award for general damages to a total \$540,000; within this total it allowed \$100,000 for pain and suffering, reducing the lower court award of \$200,000. In two other appeal cases, the maximum allowed for pain and suffering was maintained at \$100,000.² By so doing the Supreme Court established \$100,000 as the new standard in Canada for pain and suffering awards.

A pure no-fault system, in applying standards of consistency and objectivity, might exclude recovery for non-economic losses, such as pain and suffering. Arguments against compensation for intangibles such as pain and suffering state that there is no "market" or objectively determined value for an award for non-economic loss. While the courts have over the years developed relatively uniform values for awards for similar injuries, these awards

1. *Globe and Mail*, "Supreme Court Asked to Put Price on Body", April 28, 1977.

2. See *Thornton v. S. Dist. No. 57 Bd. of S. Trustees*, (1978) 1 W.W.R. 607 (S.C.C.); *Andrews v. Grand & Toy Alta. Ltd.*, (1978) 1 W.W.R. 577 (S.C.C.); *Arnold v. Teno*, (1974) 7 O.R. (2d) 276; 11 O.R. (2d) 585; S.C.C., January 19, 1978.

are basically arbitrary, and there is no clearly defensible way to determine whether they are equitable, in the sense of being adequate or necessary to the injured party's physical and mental well-being.

Nevertheless equity means different things to different people. Many persons maintain that equity is destroyed in individual cases when recovery for non-economic losses is eliminated or reduced; others explain that equity is achieved only in the case of "payment for a thing taken away". Compensation for non-economic loss, they contend, is "solace for a condition created" and not of real use in restoring the injured party to the same position he was in before the injury.

As a result, there is continuing disagreement over whether a pure no-fault plan should totally deny claims for non-economic loss. It is especially difficult to defend a compensation approach which does not provide recovery for such loss, if there appears to be prevalent among the insured public an expectation of compensation to ease the pain of injury.

Concessions are made in some no-fault proposals to the real but intangible nature of non-economic loss, by providing lump-sum payments to injured persons up to a maximum dollar amount, depending on the degree of injury. These allowances are "nominal", generally apply to serious injury or permanent loss, and fall well below many awards for comparable injuries paid under tort law to the innocent victim. In addition, they do not distinguish between victims except on the basis of injury. Examples are provided in Table 7 of Appendix A.

It is possible to have a first-party (each victim paid by his own insurer) system of compensation which treats each injury case as "exceptional" or "individual" in evaluating non-economic loss. But this system would not be consistent with the principle of objective standards; it would necessitate a costly fact-finding process to substantiate claims; and it would encounter the same problems of evaluating how much to pay as the current tort system experiences.

Therefore, given the principles of uniformity and objectivity, it is inconsistent that a victim would recover to the same degree for non-economic loss under a no-fault scheme as he does now under tort law.

5. Methods of Assessing Compensation Under Pure No-Fault

A pure no-fault plan provides compensation for the following categories of loss caused by death or injury:

- all reasonable medical expenses, including those related to physical rehabilitation;
- earnings-related compensation to replace actual earnings losses;

— certain out-of-pocket expenses such as: household services, funeral expenses, necessary appliances or fixtures, and other special care or services.

A pure no-fault plan compensates for current as well as future losses. It can be limited to compensate for actual loss only, for example, loss of income of wage-earners only; or it can be expanded to compensate for loss of opportunity as well, for example, loss of opportunity to earn income in the case of students, the unemployed and other non wage-earners.

In its strict definition, a pure no-fault plan compensates only for losses that can be directly measured in dollars. Under this definition, it would exclude compensation for loss of opportunity if this loss cannot objectively be measured in dollars. Likewise, it would exclude compensation for non-economic losses such as pain, inconvenience and loss of amenities.

Because of the above exclusions, the strict no-fault plan has often been accused of being discriminatory—that is, it discriminates against the young and old who have no earnings, and against those injured persons who suffer real pain or inconvenience.

Typical categories of loss reimbursed under a no-fault compensation system are reviewed below. Specific provisions or proposals in other jurisdictions are discussed in Section H and illustrated in detail in Appendix A.

Non-Economic Loss

As already discussed, when concessions are made to paying some amount for “pain and suffering”, compensation is usually determined on the basis of a schedule of benefits related to degree of injury. Lump sum allowances are provided within a pre-determined maximum. There may be no provision for pain and suffering benefits in the case of minor injury.

Economic Loss

For economic loss, the pure no-fault system first defines the categories of loss eligible for compensation and the characteristics of the victim or his family to be considered in setting the amount of compensation. In addition, the maximum level of “reasonable” or allowable compensation is normally pre-determined to meet essential needs first.

In this regard, medical and rehabilitation expenses are considered to be essential and are typically covered for an unlimited amount under a pure no-fault system. The no-fault approach to wage loss indemnity in various situations of full or partial loss is described in further detail below.

Wage Loss

Indemnity for wage loss under the no-fault system is typically made available for an unlimited period of time, for as long as disability continues.

However, a no-fault system normally specifies some limit to the total amount of weekly or other periodic indemnity payable. Table 3 of Appendix A provides examples of provisions for wage loss in several existing plans or proposals. A description of three general approaches to payment of wage indemnity follows below.

- a) Payments at a flat rate for everyone, regardless of earnings lost.

The main disadvantage of this method is that it penalizes those who have lost more; and can be overgenerous to those who have lost less. A flat rate sufficient only for the basic necessities of life will penalize a major proportion of accident victims; conversely, a flat rate with generous benefits could make prolonged disability more attractive than rehabilitation to a large segment of the population.

- b) Earnings-related payments to replace all lost income.

The primary objection to a benefit scheme which pays 100% of earnings to *all* injured persons is high average cost. Under the liability system only the *innocent* victim is entitled to full earnings recovery. Extending full recovery to all victims not only obligates each motorist to share in the insurance cost of compensating all injured persons, it also obligates him to compensate the high income earner at a high level of wage indemnity. As a result, low income earners may be forced to pay a higher average premium level, designed to allow full recovery by the wealthy.

- c) Earnings-related payments to replace *part* of lost income; indemnity computed as a standard fraction of the earnings lost, or subject to a maximum eligible wage level.

Reduction of earnings-related benefits by a standard fraction, for example 10%, is intended to prevent overcompensation, by ensuring that deductions such as tax are netted out. Indemnity at below actual income can also serve as a deterrent against fraud, self-inflicted injury or malingering, as well as provide an incentive to rehabilitation. However a standard fraction reduction may penalize the low wage-earner such that this factor may need to be adjusted at lower wage levels.

A limit set on the amount of wage loss benefits payable on a weekly, annual or other periodic basis is another common approach to no-fault compensation. For example, income replacement can be guaranteed to meet the weekly wage losses of either an average wage-earner, or of a major proportion of residents, say 85%. Automatic increases in the maximum eligible wage to correspond to cost of living increases should be incorporated.

Any person who feels he needs protection against loss of income in excess of the guaranteed level, would have to procure this protection on a voluntary basis. In this manner, costs of providing income replacement insurance are kept at an average or acceptable level. Wealthier individu-

als, desiring full earnings-related benefits, are expected to be able to afford the purchase of additional coverage.

In the choice of the method of compensation for wage loss, consideration should be given to whether a one-tier or two-tier system will exist for insurance coverage. In a one-tier system, a single mandatory scheme of compensation is designed to serve all accident victims. In a two-tier system, a mandatory scheme of basic benefits co-exists with a market for higher benefits, thereby allowing motorists to voluntarily extend their coverage.

In considering the above approaches it is also important to recognize that persons other than the vehicle owner are protected by the level of mandatory insurance coverage. While the vehicle owner may decide to extend his wage loss recovery beyond the mandatory level by purchasing a second tier of coverage, the uninsured pedestrian he injures will recover only to the extent provided for under the mandatory coverage.

Partial Disability

Other important choices arise in structuring a no-fault plan of compensation. For example, how is compensation to be paid in cases of partial disability? Some common approaches follow:

- a) Partial income replacement pre-determined on an arbitrary basis: for example, 50% of total disability payments.

This method discriminates against those whose earnings under partial disability are less than the arbitrary percentage of their normal earnings, and it favours those who earn more than the given percentage of their normal earnings.

- b) Partial income replacement based on medical assessment of degree of disability. That is, indemnity is provided as a medically determined percentage of normal earnings.

It should be noted that a person assessed as 45% disabled, may be unable to find any employment during his partial disability, but would only receive 45% of his normal earnings as indemnity under this method.

- c) Income replacement in excess of any actual earnings during period of partial disability.

This method may be difficult to administer, as it relies on the injured person to report any earnings during a period of partial disability. However, it appears to be the most equitable approach to indemnifying the partially disabled.

Compensation of the Non-Earner

Another matter to be dealt with under a no-fault plan of compensation is the question of the non-earner. The common law system of evaluating

damages takes into account such factors as past employment, education, age, sex, family responsibilities, and potential for future earnings in assessing damages for non-earners such as students, minors, the unemployed, and stay-at-home spouses. A pure no-fault scheme that ignores the non-earner entirely is unlikely to be acceptable to the public as an alternative to the current reparations system.

Several approaches are available to compensate the non-earner in a relatively objective fashion:

- Cover only actual expenses incurred, such as medical expenses, rehabilitation cost, actual child care costs or housekeeper services.
- Cover expected replacement expenses, such as cost of a housekeeper, without the need to prove actual expenditures for these services.
- Base compensation on previous earnings, for example in the case of the unemployed.
- Base compensation on "notional" earnings, such as the minimum wage; for example, for persons with no recent earnings history, such as students or retired persons.
- Pay compensation for short periods of time only, at a "nominal" level.
- Reserve compensation for persons who are severely injured or with prolonged disabilities.

TABLE 2
COMPARISON OF DEATH BENEFITS
ONTARIO AND NEW ZEALAND

Marital Status of the Deceased	Surviving Family	Accident Benefits Coverage, Ontario		New Zealand Accident Compensation
		Current	Effective July 1978	
Married	Wife and 4 children	\$9,000	\$14,000	\$2,500, plus up to \$15,000/yr. (gross)
Married	Wife only	\$5,000	\$10,000	\$1,000, plus up to \$7,800/yr. (gross)
Married	Husband only	\$2,500	\$10,000	Nil, supplementary plan
Widower	3 children	\$7,000	\$13,000	\$1,500, plus up to \$7,800/yr. (gross)
Single, Age 17	Parents	\$1,000	\$ 2,000	Nil, supplementary plan
Single, Age 23	Parents	NIL	NIL	Nil, supplementary plan

Death Benefits

A pure no-fault system, as already mentioned, avoids a fixed sum approach to compensation. In order to allow for the diversity of family circumstances, an earnings-related method of compensation is preferred.

It should be noted that under the terms of the standard automobile insurance policy—Section B—Accident Benefits, insurers in Ontario presently pay no-fault benefits to surviving family members in the form of fixed-sum amounts that differentiate somewhat between size of family. However, these fixed-sum amounts are entirely arbitrary and it is expected that the family will receive full consideration of its circumstances if it is eli-

gible for recovery under liability coverage within the provisions of the Fatal Accidents Act.

Under a pure no-fault system, there is no recourse to third-party recovery in death situations, so that the first-party method of compensation must provide as much flexibility as possible. New Zealand, for example, decided to provide a fixed-sum amount as an immediate payment to the surviving family to be accompanied by weekly indemnity payments related to the earnings-related compensation the deceased would have received had he/she lived, but been totally incapacitated. An example of the first-party benefits provided in Ontario compared to benefits in New Zealand is shown in Table 2.

A Sample Pure No-Fault Proposal

The above examples of alternatives for payment of economic loss under a no-fault scheme of compensation serve to illustrate that there are no easy solutions towards finding an objective and consistent method of compensation that is equitable to all. The pure no-fault approach calls for reforms to the method of compensation but leaves open a wide range of alternatives regarding the best method of compensation.

An example of a pure no-fault approach to compensation by category of loss is outlined below.

Damages	Amount of Compensation
1. Medical Expenses	Unlimited
2. Out-of-pocket expenses	\$5,000 limit; \$1,500 priority for funeral expense
3. Loss of wages or support, <i>from injury or death of wage-earner*</i>	
(a) Basic Level—injury of person with no dependants	80% of income, paid monthly, up to a maximum \$12,000 per year, gross.
(b) Supplement for Dependent Spouse (non-earner)	As above, maximum increased to \$15,000 per year, gross
(c) Supplement for Dependent Children	As above, maximum increased by \$1,000 per year, gross, per child, up to 5 children
4. Loss of services or opportunity, <i>from injury or death of non wage-earner*</i>	
(a) Housekeeper Spouse (death or injury)	Up to \$150/week for 5 years with receipts; otherwise minimum wage
(b) Others (injury only)	Level of benefits from unemployment or pension schemes to be assumed by insurer if eligibility expires while disability continues. Injured students compensated in cases of prolonged disability only, at average wage level of Jurisdiction.
5. Non-Economic Loss	No compensation

* For five years; if disability is serious or prolonged, compensation is continuous at basic level; in case of death, for five years or until remarriage, whichever occurs sooner.

6. Summary

Pure no-fault proposes to compensate all victims with security, efficiency, and equity. However, it does not clearly define which losses properly fall under a compulsory no-fault plan. Given the acceptance of the no-fault principle, three major issues must still be resolved by authors of a pure no-fault scheme of compensation:

1. Should indemnity for pain and suffering be retained? If so, should arbitrary payments be made on the basis of a schedule? Or, should there be a case-by-case analysis of awards? In this case, should recourse to the courts be retained to evaluate quantum but not liability?
2. Should benefits under a compulsory plan be paid at a minimum or at an average level of need, leaving higher coverage to be purchased voluntarily by those who want supplementary compensation; or, should the benefit plan be structured to compensate all victims on an equal pre-determined basis, without the availability of a second tier of higher coverage?
3. Should non-earners be compensated as well as earners for economic loss? To what degree?

These matters are not easily answered as they depend on value judgments and on economic factors such as the cost of specific no-fault benefits. Further consideration is provided in the remainder of this study to factors pertinent to the structure of a pure no-fault plan. In particular, Section H reviews specific no-fault provisions or proposals in other jurisdictions which illustrate ways to construct a no-fault scheme.

E. OTHER CONSIDERATIONS WITH REGARD TO NO-FAULT COVERAGE FOR MOTOR VEHICLE INJURIES

Removal of the third-party system of recovery and the substitution of settlements on a first-party or no-fault basis has a number of other consequences which are briefly outlined in this section. While the following discussion places emphasis on no-fault coverage for bodily injury, *many of the same considerations are applicable to property damage coverage* and in some cases are examined further in Section I.

1. Judging The Performance of the Insurer

Under the third-party liability system, the insurer pays claims on behalf of its policyholder to another party. The policyholder is seldom concerned about the efficiency of his insurer in reimbursing a third party. Although he implicitly pays through his premiums for the performance of his insurer in controlling claims handling costs, it is impossible for him to determine in most cases whether a premium higher than that of a competitor means better service or poor efficiency.

In a two-party system, the insured driver has a better opportunity to assess both price and service offered by his insurer. An insurer with low premiums may also be very slow in paying out losses. An insurer with higher premiums may have a more generous attitude toward claims and a larger staff to process claims quickly. The consumer of first-party insurance is able to purchase with these factors in mind.

2. Awareness of the Limits of Coverage

In a system of third-party settlements, not all policyholders recognize the need to protect themselves adequately against liability suits. The same is probably true in a system of first-party benefits—many drivers consider the possibility of serious personal injury to be remote. But the consumer of first-party insurance, through a gradual educational process, will recognize that he must look after himself by buying coverage sufficient to meet his needs for compensation, because there is no other method of recovery. In the meantime, mandatory basic coverage will serve to protect him and others injured by his car.

With better awareness, it is argued that the consumer will shop around for increased coverage when the basic package of mandatory benefits fails to meet his needs or becomes outdated because of changing social conditions or increases in the cost of living. Private insurance companies could then compete in providing extended coverage at the best price.

While basic benefit levels might be slow to change because of the need for legislative action, drivers might voluntarily seek out higher average benefits, much in the same way that many now seek out liability coverage in excess of mandatory limits. Consequently, a flexible system of compensation could develop.

3. Fraudulent Claims

Under the liability system, negligence must be established as the basis for recovery of losses. Under no-fault, injuries suffered in unwitnessed accidents are eligible for benefits. It is therefore relatively easy to represent claims for injuries suffered in other types of accidents as auto-related. It can be argued that this observation points out the need for a comprehensive system of accident and sickness compensation. However, if reform of the auto reparations system is isolated, then effective methods of control must be established to discourage fraudulent claims.

4. Merit-Rating and Surcharges

Merit-rating under a no-fault system would refer to premium discounts or surcharges associated with the number of claims submitted within a stated period of time. At present, the insurance industry in Ontario often uses a driver's accident claim record as a rating criterion, and it also applies premium surcharges based on the driver's offence record.

Under a no-fault system, use of a driver's claim record as a rating criterion or as the basis for surcharges penalizes the driver who submits claims for accidents that are not the result of his fault. Although merit-rating based on claims frequency can serve a function by discouraging abuse of the no-fault system, other methods of controlling overuse appear to be preferable as they affect fewer drivers adversely than a system of merit-rating.

Premium surcharges based on a driver's chargeable offence record are not entirely inconsistent with the functioning of a no-fault plan, as fault is determined outside the auto reparations system. Surcharges may be desirable as a means of imposing a higher total premium burden on the careless driver. The primary objection to use of driver offence records in determining no-fault premiums is that surcharges may not be applied uniformly to all relevant drivers. Therefore, the objective of equity in a pure no-fault system might not be met.

5. Subrogation Between Insurers and by Collateral Benefit Sources

Insurance companies can only subrogate by assuming the common law rights of the people on whose behalf they make payments. No-fault removes the right of the individual to common law action and, as a result, the insurer also loses that right.

Should the right of the insurer to subrogate be retained under some form of mixed fault/no-fault system, insurers would be in a preferred position to the public who are denied the right to sue. Furthermore, some insurers might voluntarily stop subrogation to derive the benefits of reduced investigative expense; while others might continue to subrogate and base lower rates on recovery of payments, creating unfair competition for insurers who absorb all their own losses. Representatives of the Insurance Bureau of Canada have stated before the Select Committee their belief that the law of averages would equalize most no-fault claim payments among insurers without the need for subrogation.¹

Under a uniform system of no-fault, the right of subrogation by the Ontario Health Insurance Plan or other public collateral benefit sources should also be abolished, otherwise fault determination is reintroduced. At the present time in Ontario, "innocent party costs are borne by the automobile insurance system while negligent party costs are borne by the health insurance system."² If it is deemed necessary to make the auto insurance system responsible for *all* losses from motor vehicle accidents, then a system of repayments pro-rated among insurance companies can be introduced to reimburse these benefit sources on a no-fault basis. This matter requires separate study, preceded by a decision by legislators that motorists should bear all

1. Proceedings of the Select Committee on Company Law, remarks by Mr. C. Fraser on behalf of the Insurance Bureau of Canada, August 18, 1977.

2. Woods, Gordon & Co., Report IV to the Select Committee on Company Law, "Processing of Claims by the Insurance Industry", March 1977, page 60.

costs of motoring. The question of primacy of insurance coverages was discussed briefly before in Section D.

6. Benefits for Non-residents and Out-of-Province Coverage

The typical approach to coverage for non-residents injured in the Province is as follows. Under a no-fault system, non-residents would be limited to recovery of benefits to the extent that they are not at fault for the accident, and to the extent payable under the mandatory no-fault plan. That is, non-residents would not be able to sue for recovery in excess of the bodily-injury benefits available in the no-fault jurisdiction; otherwise non-residents would be afforded a right not available to residents. Some method of informing the non-resident of his coverage in the no-fault jurisdiction would be required; this is particularly important in areas where non-resident traffic is high.

Residents named under a no-fault policy would typically be entitled to full no-fault benefits whether injured outside or inside the Province. This protection could be extended to all residents in the event, say, that an uninsured person is involved as a pedestrian in an automobile accident outside the Province. Residents would however be allowed to sue outside the Province for excess amounts, if any, that might be awarded under the law of the jurisdiction in which the accident occurs.

Should the resident of the no-fault jurisdiction be at fault in an accident in a jurisdiction where liability laws apply, the no-fault package would also need to provide ancillary coverage equivalent to that required as evidence of automobile liability insurance under the financial responsibility laws of the place in which the injury or damage occurs.

7. Rating

Under a system of third-party liability payments, the insurer does not know whom his insured will injure. Nor is he responsible for paying the claims of his own insured, as the liability for payment falls on the insurer of the party at fault (except to the extent of Accident Benefits coverage). Because the risk assumed by the insurer is random, the characteristics of the injured person are ignored as a factor in rating.

In contrast, under the no-fault system, the insurer is in all cases accountable for paying the claims of his own insured. Depending on the type of victim-insurer relationship as discussed in the next section, the insurer may also assume responsibility for payment of the claims of relatives of the policyholder, occupants of the insured vehicle, and pedestrians.

With the payment of losses established on a first-party basis, an insurer can more readily identify the potential claimant, and can base the rates he charges on two elements of the risk of loss: how often claims will be pre-

sented (frequency); and, how much will be paid (severity or average claim cost).

In addition, categories of loss can be assessed separately in setting rates. For example, it is possible under a no-fault system to consider death benefits separately and to charge a lower premium rate to a single driver with no dependants.

There is however the possibility that the burden of insurance cost will be shifted, perhaps adversely, from classes with high accident frequency, such as young drivers, to classes with high recovery expectations, such as older drivers with large families. Concern also exists about possible changes in the methods of risk selection in a first-party system. While the middle-aged family man may now be a preferred risk, he may become an undesirable risk if the potential size of his loss is taken into account.

There is no doubt that some redistribution of premiums will occur. However, a combination of frequency and severity in rate setting could well result in lower rates for the more experienced, careful driver compared to higher rates for the reckless or inexperienced driver. In any case, under first-party insurance, what the policyholder receives in the way of benefits can be more closely related to what he pays for in the way of premiums.

8. Insurance Coverage

Victim-Insurer Relationship

By substituting first-party compensation for payment on the basis of fault, the pure no-fault system does not automatically guarantee compensation to every victim. For the victim who does not own or drive a vehicle, some relationship must be set up between the victim and the insurer to secure compensation.

The 1974 Inquiry on Automobile Insurance in the Province of Quebec outlined three possibilities for a workable relationship:

“The coverage can be on the family, the motor vehicle or the driver. In the first case, the insurance protects all the members of the same family, regardless of the motor vehicle in which they are travelling or by which they are struck. In the second case, the insurance covers the vehicle and compensates the occupants and any other victims. The third case provides that the insurance is tied to the driver.”¹

One major factor guiding choice among these three alternatives is the ability to enforce compulsory insurance. Family coverage, because there are many families with no car, would be most difficult to control. Driver insurance increases the number of persons to be insured and extends enforcement

1. Government of Quebec, *Report of the Committee of Inquiry on Automobile Insurance*, Jean L. Gauvin, Chairman, March 1974.

problems. In addition, both family and driver insurance potentially increase the number of parties involved in an accident, as each injured person deals with his own insurer. Handling of applications for compensation becomes more complicated.

Coverage based on ownership of the motor vehicle appears to be the least troublesome way of paying compensation under a no-fault system. Compensation would be provided to all occupants of the vehicle, pedestrians, and any other person injured by the insured vehicle.

A further factor to be considered in choosing an appropriate victim-insurer relationship is the matter of rating. No-fault bodily injury coverage based on the vehicle or on the driver is more likely to be charged at an average flat premium rate than is family coverage. The insurer does not know whom his insured will injure, such that the characteristics of this category of claimant may be ignored in rating. Family insurance, on the other hand, is by its nature suited to greater differentiation in rate setting as the characteristics of the potential claimant are readily identified.

As indicated in the previous section, the insurer knows under all three alternatives that he must cover the claims of the driver or principal operator of the vehicle and may rate accordingly.

Accidents may still involve uninsured vehicles, or unidentified vehicles, as in hit-and-run accidents. Therefore, provision still needs to be made under a no-fault scheme for a Fund to indemnify victims in these situations.

Vehicles Insured

If coverage is to be related to the vehicle, the principal of universal compensation also requires that motor vehicles other than passenger cars be included under compulsory no-fault coverage. Otherwise, the right to sue must be retained for persons injured by these vehicles.

Exclusion of non-passenger cars from no-fault would create an unfairly discriminatory situation. For example, persons injured by a truck or motorcycle would be able to collect full damages, including pain and suffering, based on a court assessment; whereas persons injured by a passenger car would be subject to the recovery rules of the no-fault compensation scheme.

The major objection raised to inclusion of other types of motor vehicles under no-fault is the problem of setting rates. For example, under no-fault, the commercial vehicle becomes an attractive risk for the following reasons: a large commercial vehicle suffers less damage in a collision than a passenger car; the driver of the commercial vehicle usually suffers less injury; there are usually fewer passengers in the vehicle; and the driver is often covered by Workmen's Compensation which may take precedence over no-fault

benefits. Under the tort system, the commercial vehicle is a less attractive risk and is assessed a high premium, because of the greater potential for injuring other people.

The opposite situation is true for motorcycles. Motorcycles under no-fault tend to be assessed high rates because their drivers are vulnerable to serious injury.

Objections to the rating situation outlined above have resulted in exclusion of non-passenger vehicles from compulsory no-fault provisions in several U.S. states, notably Michigan.

Solutions to the rating problem can perhaps be found. A 1971 bill before the U.S. Congress suggested that:

“The Secretary of Transportation shall classify all motor vehicles larger than ordinary passenger automobiles into reasonable categories; and shall assign to each category a percentage of responsibility for net economic loss sustained by occupants of other vehicles; such classification and percentages of responsibility shall be based upon the increased severity of injury caused by large vehicles in comparison to ordinary vehicles.”¹

Other solutions include the imposition of absolute liability on the part of commercial vehicle owners. That is, they would be responsible for all losses in accidents involving their vehicles, regardless of fault and regardless of the no-fault coverage of other persons involved in the accident. It is inconsistent under pure no-fault to leave non-passenger cars under the negligence system; however, in a number of jurisdictions these vehicles have been excluded from no-fault provisions.

9. Breach of Condition

Present no-fault Accident Benefits coverage can leave the insured person uncompensated by reason of a breach of condition in the policy. This is primarily a punitive measure designed to exclude from compensation drivers guilty of certain offences against Highway Traffic or Criminal Code regulations.

The Ontario standard automobile policy lists the following factors as a breach of condition under Section B—Accident Benefits:

- a) The insurer shall not be liable under this section for bodily injury to or death of any person:
 - (i) resulting from suicide of such person or attempt thereat, whether sane or insane; or

1. U.S. Congress Senate Committee on Commerce, *National No-Fault Motor Vehicle Insurance Act*, Report No. 891, 92nd Congress, Washington, 1972.

- (ii) who is entitled to receive the benefits of any workmen's compensation law or plan; or
 - (iii) caused directly or indirectly by radioactive material.
- b) The insurer shall not be liable under subsection 1 or Part II of subsection 2 of this section for bodily injury or death:
 - (i) sustained by any person who is convicted of drunken or impaired driving or of driving while under the influence of drugs at the time of the accident; or
 - (ii) sustained by any person driving the automobile who is not for the time being either authorized by law or qualified to drive the automobile.

In a similar manner, pure no-fault proposals may exclude coverage for persons under the influence of drugs or alcohol, or for injuries that are self-inflicted or sustained while being involved in excluded or illegal activities. However, persons injured by the excluded motorist would retain their right to compensation.

Some supporters of the no-fault principle dispute the fairness of the "punitive" breach of condition, because, in practice, persons other than the driver can be denied recovery. For example, the dependants of the injured driver may be denied support by refusing compensation on the basis of impaired driving or other breach of condition. And, just as in the general argument against the liability system, it is maintained that refusal of compensation on the basis of indictable offences is unlikely to persuade drivers to drive more carefully.

"Fault" Deductible for Bodily Injury

In order to retain the "punitive" aspects of breach of condition, without denying needed compensation, proposals have been put forward for a type of "fault" deductible for bodily injury. Under certain situations such as infractions to the Highway Traffic Act or Criminal Code offences, recovery of a deductible of \$500, \$1,000 or more is denied to the "guilty" driver.

The deductible approach does create a problem of delay, as insurers may hesitate to pay compensation until infractions or offences are established in the courts. This might serve to delay compensation of innocent people. A possible although round-about remedy has been suggested, whereby the courts are given the right to impose a fine equivalent to the deductible amount, to be paid back to the insurer.

10. Appeal or Review Procedure Under Pure No-Fault

A pure no-fault system must retain a method of appeal for the victim who believes he has been wronged by the amount of compensation provided by his insurer. Yet a primary goal of the no-fault system is to take compen-

sation claims out of the courts, therefore an alternative appeal procedure must be established.

Disputes arising under the no-fault system are likely to centre around contractual issues. For example, an insurer may deny payment by reason of breach of condition, claiming that the driver was impaired at the time of the accident. Similarly, an insurer may deny payment, claiming the injury was the result of a previous condition and not directly the result of the automobile accident.

An appeal mechanism to handle such disputes might be established outside of the insurance industry in order to guarantee impartiality. In New Zealand, where a no-fault compensation scheme is in operation, the appeal procedure starts with a number of internal reviews, followed by appointment of a hearing officer if the claim is still denied. The hearing officer has the power to summon witnesses, administer oaths and hear evidence. Decisions are delivered in writing, and costs may be awarded. Appeal of this decision can be carried onto a public Accident Compensation Appeal Authority. On questions of law or regarding issues of general public importance, a right of appeal is given to the Administrative Division of the Supreme Court or ultimately to the Court of Appeal Division.

In New Zealand, and under any pure no-fault system, appeals are normally undertaken to reverse a decision denying a claim. The appeal procedure does not independently assess the value of damages payable to the claimant. Valuation is based solely on the categories of loss covered in the no-fault insurance contract, unlike the tort system where categories of loss and the value of damages can be defined by the court.

Rather than inserting a stage of adjudication into the appeal procedure, direct recourse to the courts can be allowed to settle contractual disputes. A common criticism of no-fault pertains to this method of appeal. It is maintained that insurer-insured court cases will grow in number under no-fault, negating the goal of taking claims out of the courts.

Design of the compensation system will influence the relative importance of whatever type of appeal mechanism is established. Realistic benefits that cover all economic classes of claimants reduce dependence on the right of appeal. Administrative efficiency in processing claims and decisions delivered in writing are also needed to reduce frustration and to put the claimant as quickly as possible in a position to appeal if it should be necessary. If an adjudication procedure is adopted to handle disputes, then decentralization is essential to provide for ready access by all auto accident victims.

11. Summary

In summary, this section has presented a number of further considerations related to no-fault coverage. It has addressed itself to the advantages of

no-fault with respect to the claimant's increased ability to judge the performance of his insurer and his increased awareness of the limits of his coverage.

In addition, this section has indicated that a no-fault approach will require the consideration of new methods of rating; increased emphasis on effective control of fraudulent claims; a review of the methods of merit-rating and surcharging; the coordination of coverage with collateral benefit sources to ensure that auto insurance is the first payor; a review of coverage for non-residents and for out-of-province accidents; and the consideration of whether no-fault insurance should follow the vehicle owner, the driver or the family unit.

In considering the moral and legal principles underlying the no-fault system, two further issues were noted in this section, namely:

- Should a no-fault plan, in whatever form it is adopted, exclude coverage to persons guilty of certain offences against traffic or criminal code regulations?
- Should an appeal procedure be established outside the insurance industry to aid in adjudicating disputes over payment of claims? Should this appeal procedure remain within the courts (as it is under the tort system), or should it be established outside the court system?

F. A COMPROMISE APPROACH: NO-FAULT WITHOUT ABANDONING THE FAULT CONCEPT

In response to evidence demonstrating the many unsatisfactory results of the fault/liability system, a growing number of jurisdictions have introduced no-fault features into their automobile accident reparation systems. To date, only New Zealand has substituted a pure no-fault compensation plan and completely eliminated tort recovery in the area of bodily injury. However, the Province of Quebec has recently passed legislation to introduce a similar pure no-fault scheme for bodily injury, with implementation on March 1, 1978.

In the remaining jurisdictions, strong arguments on behalf of retaining the tort system, and concerns about pure no-fault as a substitute reparations system have encouraged compromise solutions to compensation. These arguments and concerns are outlined below, followed later in this section by a review of various compromise approaches to compensation.

1. Major Issues in the Fault/No-Fault Debate

In Defence of the Fault Concept

The supporters of the fault system defend tort recovery over no-fault recovery for a number of strongly-argued reasons. A brief review of key arguments on behalf of the fault concept are presented here.

A key defence in advocating retention of the tort system is related to a matter of principle. The aim of recovery based on fault is to *guarantee the innocent victim full indemnity*. Critics of no-fault argue that it is unjust to substitute an average level of compensation available to all injured persons, for full recovery by the innocent victim. Compensation to other victims must be secondary and will be dependent on the resources of the community.

While pure no-fault proposals may reduce or contain costs, generally they do so only through reduction of coverage and benefits to the innocent victim. It is rightfully argued that it is impossible under a pure no-fault system to compensate all injured persons at the standard afforded to the innocent victim under the tort system without a substantial increase in cost to the insured driver. This statement is illustrated further in Section G.

Following from this concern about the innocent victim, is a second defence: the fault system provides a mechanism for *recovery of loss to the fullest extent possible*. Under the tort system, the innocent victim is compensated both for measurable damages and for intangible non-economic loss. Furthermore, the tort reparations system provides recourse to judge and jury to assess both the extent and nature of loss. Court assessment of damages is held up to be the most complete and adaptable method of determining the full value of the complex losses resulting from bodily injury.

A pure no-fault scheme, which discards payment for non-economic loss, is considered to be second-best, because it sacrifices a possibly legitimate class of loss for the sole reason that it "frustrates precise measurement and defies an efficient system of reimbursement". A pure no-fault scheme which retains payment for intangible loss is still considered to be second-best, if it assigns arbitrary awards based on degrees of injury, without differentiating between individual cases.

A further argument in favour of the fault system is that it provides a *well-established adversary mechanism* for dealing with disputes over the amount of a settlement. A claimant unsatisfied with the settlement offered to him can hire expert counsel to protect his interests and bring his case before a court for final assessment. Basic to the elimination of the fault system is the substitution of a non-adversary reparations method which also satisfies the claimant that he is being equitably reimbursed.

However, pure no-fault raises a two-fold concern among advocates of the adversary system. First, it is argued that the claimant will be in a weaker bargaining position under the no-fault system, relative to the trained adjuster who will tend to settle claims in favour of the insurer rather than the insured. Secondly, it is said that pure no-fault will encounter some of the same problems that occur under a Workmen's Compensation system. While no-fault, like Workmen's Compensation, does not require the determination of fault, it does call for judgement on other contested issues, such as degree of dis-

ability and the cause of an injury, whether it arose out of a motor vehicle accident or resulted from a previous condition. For these two reasons, advocates of the adversary system argue that no-fault claimants will demand an effective dispute handling procedure, and they are unlikely to find any other appeal mechanism which is as impartial or open to individual circumstances as the existing court system.

Another frequent defence in advocating retention of the tort system is that a recovery process based on tort *encourages responsibility* and provides punishment for negligent conduct. Yet, *given the existence of insurance coverage*, preservation of the fault system is difficult to defend based only on the notion that the motoring public believes that the careless driver is in fact being punished for his negligence. Rather, the public is perhaps more apt to ask: Why should 90% or so of vehicle owners in the Province alter their driving behaviour if they know they can turn to the liability system of insurance to pay the "bills" for the damage they cause?

Concern About the Economic Repercussions of Pure No-Fault

Aside from the moral arguments over the fault concept and the complex issue of intangible loss, many reformers of the automobile compensation system seek a retreat, at least temporarily, from pure no-fault for a number of pragmatic reasons. Four common motives for a retreat to a compromise solution, and salient comments regarding their validity in Ontario, are presented below:

1. Pure no-fault is an innovative and radical step: there is insufficient information available on the nature of auto accident injuries and on the characteristics of the injured person to properly evaluate the repercussions of no-fault, and more importantly, to cost it.

This concern is applicable not only to a pure no-fault system but to any mixed fault/no-fault plan with a significant level of first-party benefits. Michigan is an example of one jurisdiction which has enacted no-fault legislation providing for relatively generous no-fault benefits. (Refer also to Section H.) Insurers in that state were confronted in 1972 with the necessity of developing costs to accommodate the no-fault laws. Their initial cost calculations were not exact; adjustments are still being made to account for inflationary factors and to take account of developing loss experience. Although the Michigan leap into no-fault is still considered to be experimental by some, others are considering it to be a permanent success, as it has achieved a number of important reforms in the method of compensation, without completely disrupting the insurance industry.

2. Compulsory pure no-fault will destroy competition and precipitate concentration in the private insurance industry. Only industry giants or a public monopoly will be able to survive the reorganization and achieve

the savings demanded by pure no-fault.

With respect to this second argument, reorganization to accommodate pure no-fault will require industry cooperation. It is unlikely that smaller insurance companies will be able to switch smoothly to a total first-party mode of rating and distribution of benefits without a pooling of knowledge and expertise. However, this pooling can be accomplished under an industry umbrella organization such as I.A.O. Hence the necessity of sharing knowledge need not precipitate industry concentration.

3. Lifetime or unlimited benefits under pure no-fault will create problems of reinsurance, particularly for smaller companies, and they will aggravate the possibility of risk rejection by the voluntary market.

Smaller insurance companies may also be troubled by the problem of large or unlimited risks under no-fault.¹ Lifetime benefits or unlimited medical coverage extend the exposure of small companies since they are unable to spread this risk across a large block of business. Typically they must reinsure all or a portion of the risk with another insurer, in order to keep overall risk in line with their relatively small capital position. Reinsurers in the United States, for example, have priced reinsurance on unlimited no-fault claims at levels which place the small companies at a competitive disadvantage relative to larger companies, who retain most of their own risks. One of the solutions advanced is to provide the means for insurers to pool exposures above a certain limit and pay benefits out of a central fund.

The uncertainty of unlimited risks is also a problem under the fault system when liability coverage is made an unlimited amount. In either the fault or the no-fault situation, the possibility of large exposures affects the risk selection policies of both small and large insurance companies. However, under pure no-fault, rejection of a risk may be more common, as identification of poor or large risks is more accurate on a first-party basis.

It should be noted that, in Ontario, insurers do not rely on the reinsurance market to the extent observed in the U.S. Under no-fault in this Province, potentially large risks are likely to be handled as "residual" business; accordingly, benefits in these "high exposure" situations would be payable out of a central fund, such as the Facility.

An alternative approach to handling the market repercussions of no-fault is illustrated by the decision recently made in the Province of Quebec. To prevent risk rejection and the consequent expansion of the residual market, and to ensure the availability of benefits on a lifetime or unlimited basis, the Province of Quebec has decided to designate operation of its newly legislated reparations system for bodily injury to a government corporation.

1. U.S. Department of Transportation, *op. cit.*, 1977, p. 78.

4. Pure no-fault will have a severe economic effect on the livelihood of lawyers, agents, and independent insurance adjusters.

Finally, it is argued that pure no-fault is an extreme solution that will have a severe economic effect on the livelihood of lawyers, agents, and independent insurance adjusters. In the recent submission of the Advocates Society in Ontario, the Committee was told that the legal profession in the Province would not be severely affected by elimination of tort rights in the case of motor vehicle accidents.¹ The legal profession in this Province apparently does not rely on motor vehicle litigation to the same extent as in many U.S. states, such as California where the Committee was told that motor vehicle litigation is the "bread and butter" of many lawyers.

The effect on the agent of introduction of pure no-fault is difficult to predict without consideration of the specific methods to be employed for marketing and distributing no-fault insurance. However, the role of the independent adjuster is likely to be seriously affected by a reorganization to a full first-party method of distributing benefits. Insurers would pay benefits mainly to their own policyholders and would rely much more on staff adjusters. Independent adjusters could continue servicing policyholders in less concentrated market areas, but their use would probably diminish if the objective of simplifying the recovery process under pure no-fault is met. It should be noted that there is already a trend toward increased dependence on staff adjusters under the present insurance system in Ontario.

Certain of the above factors are, in large part, political concerns. They would perhaps be left to the government of the day for consideration as additional factors that may or may not argue for a retreat from any fundamentally new no-fault programme.

2. The Compromise Approach

The arguments and concerns presented above have encouraged many reformers to seek a compromise solution to compensation. The compromise approach to compensation introduces the concept of mandatory first-party benefits *without* abandoning the fault concept; that is:

1. It requires that basic benefits, up to a pre-determined amount, be provided to virtually all victims of automobile accidents, quickly and regardless of fault; and
2. It maintains, to some degree, the right of the injured person to sue the person at fault for damages.

1. Proceedings of the Select Committee on Company Law, August 24, 1977, Remarks by T. H. Rachlin of the Advocates Society of Ontario.

In Ontario, Accident Benefits coverage on a first-party basis has been a mandatory part of liability insurance policies since 1972. Table 3 outlines provisions for no-fault Accident Benefits in Ontario compared to those in the other Provinces of Canada and in 16 U.S. states. The Committee, in its First Report, noted that it was convinced that "Accident Benefits coverage has been in principle a worthwhile addition to the automobile insurance system of the province".¹ The Committee recommended that a number of changes be made in the details of that coverage, increasing the amounts of benefits. This recommendation was subsequently adopted by the government which announced its intention to increase the level of Accident Benefits coverage effective July 1, 1978. A more detailed history of no-fault in Ontario and in other jurisdictions is presented in Section H.

Table 3
AUTOMOBILE INSURANCE PLANS WITH NO-FAULT
ACCIDENT BENEFITS COVERAGE
CANADA AND THE UNITED STATES**

Jurisdiction	First-Party, No-Fault, Benefits			Minimum Medical Payments (First Party-Only)				Effective Date of No-Fault
	Medical Costs	Wage Loss Benefit	Non-Work Related Benefits ⁽¹⁾	Maximum Payments (First Party-Only)				
				Medical Costs	Wage Loss	Non-Work Related	Other	
Canadian Jurisdictions								
Ontario (Comp. Act)	\$5,000	\$10/wk./104 weeks	\$1,000 + \$1,000	\$10,000 (2)	-----	-----	-----	1972 (3)
Quebec (Act on Acc. Ins.)	\$5,000	\$15/wk./104 weeks	\$1,000 + \$1,000	\$15,000 (4)	-----	-----	-----	1980 (5)
Manitoba (2)	\$5,000	\$10/wk./104 weeks	\$1,000 + \$1,000	\$10,000 (6)	-----	-----	-----	1980 (7)
Saskatchewan	\$5,000	\$10/wk./104 weeks	\$1,000 + \$1,000	\$10,000 (8)	-----	-----	-----	1980 (9)
Alberta	\$5,000	\$10/wk./104 weeks	\$1,000 + \$1,000	\$10,000 (10)	-----	-----	-----	1980 (11)
British Columbia	\$10,000	\$15/wk./104 weeks	\$1,000, \$15/104 wks., \$51,000, \$15/104 wks.	\$10,000 (12)	-----	-----	-----	1980 (13)
U.S. Jurisdictions								
Alaska	\$10,000	\$125/wk./52 weeks	\$1,000	\$10,000	\$500	52 weeks	5	Apr. 75
Connecticut	5	\$5,000	5	\$20,000,000	-----	-----	5	Jan. 78
Florida	5	\$5,000	None	\$10,000,000	-----	-----	5	Oct. 78
Georgia	\$2,500	\$200/wk., \$5,000 max.	\$1,000	\$10,000,000	\$500	18 days	5	Mar. 78
Idaho	5	\$200/wk., \$15,000 max.	5	\$20,000	\$5,000	-----	5	Jan. 75
Illinois	\$5,000	\$200/wk./52 weeks	50 weeks (14) (15)	\$15,000,000	\$500	5	5	Feb. 78
Indiana	5	\$200/wk., \$10,000 max.	50 weeks (16) (17)	\$10,000,000	\$5,000	5	5	Oct. 77
Iowa	5	5,000	5	\$20,000,000	-----	-----	5	Jan. 75
Kansas	\$10,000	\$200/wk./52 weeks	50 weeks (18) (19)	\$20,000,000	\$500	5	5	Oct. 77
Kentucky	5	\$200/wk., \$10,000 max.	50 weeks (20) (21)	\$10,000,000	\$5,000	5	5	Oct. 77
Louisiana	5	\$200/wk./52 weeks, \$10,000 max.	\$1,000 (22) (23)	\$10,000,000	\$500	5	5	Oct. 78
Maine	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Massachusetts	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Michigan	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Minnesota	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Mississippi	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Missouri	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Montana	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Nebraska	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Nevada	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
New Hampshire	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
New Jersey	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
New Mexico	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
New York	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
North Carolina	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
North Dakota	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Ohio	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Oklahoma	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Oregon	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Rhode Island	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
South Carolina	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
South Dakota	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Tennessee	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Texas	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Utah	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Vermont	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Virginia	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Washington	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
West Virginia	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Wisconsin	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78
Wyoming	\$10,000	\$200/wk./52 weeks	\$1,000	\$10,000,000	\$500	5	5	Oct. 78

* See Ontario, 1978 Insurance Policy Book, page 10.

** Figures are for 1978, unless otherwise noted.

(1) Personal benefits for non-work related injuries.

(2) \$5,000 for medical, \$10,000 for non-medical, \$10,000 for non-medical.

(3) \$5,000 for medical.

(4) \$5,000 for medical.

(5) \$5,000 for medical.

(6) \$5,000 for medical.

(7) \$5,000 for medical.

(8) \$5,000 for medical.

(9) \$5,000 for medical.

(10) \$5,000 for medical.

(11) \$5,000 for medical.

(12) \$5,000 for medical.

(13) \$5,000 for medical.

(14) \$5,000 for medical.

(15) \$5,000 for medical.

(16) \$5,000 for medical.

(17) \$5,000 for medical.

(18) \$5,000 for medical.

(19) \$5,000 for medical.

(20) \$5,000 for medical.

(21) \$5,000 for medical.

(22) \$5,000 for medical.

(23) \$5,000 for medical.

1. Select Committee on Company Law, *First Report on Automobile Insurance*, page 71.

The following discussion concentrates on presenting the general methods, advantages, and weaknesses of combining no-fault compensation with the tort system of recovery. Reference is made to the experience in the United States with no-fault laws introduced since 1971.

3. Methods of Combining Fault and No-Fault

There are two principal methods by which no-fault features have been combined with the fault concept in jurisdictions adopting a mixed approach to compensation. A discussion of these methods follows.

“Add-On” No-Fault Benefits

In a system where no-fault benefits are “added on”, first-party personal injury coverage is made compulsory as a supplementary method of recovery. In general, tort rights are fully retained except for amounts covered by first-party benefits. The objective of this approach to compensation is to ensure that minor claims for economic loss are settled by the policyholder’s own insurer. Larger claims and claims for non-economic loss continue to fall under the fault/liability system.

As first-party benefits are increased or enriched, larger claims for tangible loss fall under the first-party recovery process. The right to recovery under the fault system “moves up”, such that only a small number of economic loss claims remain under tort recovery.

In this method of mixing fault and no-fault, the right to sue can be eliminated in law for losses covered by first-party benefits, or first-party coverage can be provided without any legal restriction on tort rights (common when first-party coverage is not mandatory). Saskatchewan, for example, has changed its laws to remove the right to sue for benefits available under compulsory first-party coverage. In contrast, in Ontario, legal rights have not been changed. The right to sue for damages *including* the amounts recoverable under the Accident Benefits Section of the automobile policy is retained, but insurance companies amongst themselves have voluntarily agreed to waive their rights to subrogation for the Accident Benefits component of damages paid.

It can be said that Ontario does not have true no-fault insurance because it does not legally require that no-fault benefits for economic loss supplant liability insurance for the same loss. However insurance companies have recognized that the savings from a shift to Accident Benefits payments can only be realized by ceding the right to subrogation between first-party insurers.

Tort Restriction

In a system based on tort restriction, compulsory first-party personal injury coverage is not merely an “add-on” feature but an essential part of

the automobile insurance plan. Tort rights are eliminated for amounts covered by first-party benefits, *and* for recovery of non-economic loss except for specified circumstances.

To reiterate, this approach to combining fault and no-fault denies the right to sue for non-economic loss and then re-introduces it for specified loss situations. These situations are marked by thresholds commonly related to:

- length of disability;
- monetary amount of economic loss; or
- degree of injury.

As examples, in the following jurisdictions the right to sue for non-economic loss is given when the length of disability exceeds 180 days (Nevada); the amount of medical expenses exceeds \$500 (Colorado); or, in cases of "death and serious permanent injury, which includes substantial disfigurement" (Michigan).

As the aim of a threshold is to reduce the number of accident victims who are entitled to tort recovery, it is necessary that the level of first-party benefits paid regardless of fault adequately meet the economic losses of the majority of injured persons. Otherwise tort claims result for residual economic loss, adding unnecessary costs of fault investigation back into the insurance system.

First-party benefits can be designed to cover the bulk of measureable losses suffered by the less seriously injured; but they generally do not provide for intangible loss, therefore leaving a second type of residual claim that falls under the tort system. A threshold to tort is designed to eliminate recovery of residual non-economic loss in minor claims, thereby placing the majority of minor claims exclusively under the first-party system.

The objective of tort restriction is to realize the advantages of both the first-party and third-party systems of reparations. In the case of minor injuries, where pain and suffering is minimal or less evident, elimination of tort rights achieves savings by dispensing with fault investigation and third-party negotiations. In the case of serious injuries, with potentially greater "pain and suffering", retention of tort rights permits the seriously injured victim to collect compensation for non-economic loss and to obtain a court evaluation of damages, taking into account individual needs.

Tort restriction therefore creates two classes of benefit recipients. Those with minor injuries are compensated by their own insurer under a mandatory level of first-party benefits. Those with more serious injuries are likewise eligible for a first-tier of benefits payable by their own insurer. In addition, they are eligible for full recovery of their losses as assessed by a judge or jury *if they can demonstrate that their injury falls above the threshold, and if negligence can be assigned to another individual.*

4. Advantages of a Mixed Fault/No-Fault Approach

The main objective of mixing fault and no-fault features into an automobile insurance plan is to provide basic protection from losses to a wider group of auto accident victims, while preserving full protection for the innocent and seriously injured victim. Equally important is the aim of bringing about a shift in the distribution of claims from the less efficient third-party system to the more efficient first-party system. Such a shift is expected to reduce the amount of litigation, and to reduce the amount of time required for processing claims and receiving benefits. As a result, an increase in the ratio of benefits to premium dollar is predicted, without the need to go to a pure no-fault system.

The potential for improvement in efficiency and adequacy of compensation under a mixed system depends first on the number of claims shifted away from a third-party system of recovery to a first-party system; and secondly, on the number of claims for residual compensation remaining under the tort system. The extent of savings in a mixed system relative to a pure no-fault system is illustrated further in Section G.

In Ontario, there have been no studies conducted to indicate specific improvements in compensating victims after personal injury coverage was made mandatory for liability policies on January 1, 1972. It would seem likely that many of the advantages claimed for partial no-fault already exist in Ontario because of coverage under Section B of the automobile policy.

Table 4 does provide limited evidence of a decline in motor vehicle actions filed in the period following January 1, 1972 when changes to the Insurance Act made first-party coverage compulsory for each purchaser of liability insurance. Court statistics prior to 1972 are officially available only for the County of York Supreme Court, therefore limiting the conclusions to be drawn in the overall Ontario situation.

While there is a lack of comprehensive evidence about the adequacy or the merits of the Ontario "add-on" or Accident Benefits approach to no-fault, the advantages of a mixed fault/no-fault system have been demonstrated by recent studies conducted in Massachusetts, Florida and Michigan. These studies show that introduction of even limited compulsory no-fault benefits for personal injury has brought about a number of favourable results in these states, namely:¹

- Protection from losses due to injury has been extended to a wider group of victims, notably to persons in single-car accidents who went uncompensated under the tort system (Michigan and Massachusetts).

1. Council on Law-Related Studies, *No-Fault Automobile Insurance in Action*, Oceana Publications, Inc., New York, 1977.

TABLE 4
MOTOR-VEHICLE CASES IN THE COURTS
COUNTY OF YORK

Year	Motor-Vehicle Accidents		Supreme Court Motor-Vehicle Cases		Ratio of Actions Commenced to 100 Accidents in Previous Year **	Cars Insured in Ontario	
	Number	Increase (%)	Number	Increase (%)		For Medical Payments Coverage (million)	For Accident Payments Coverage (million)
1967	36,993	—	1,361	—	—	.94	—
1968	41,026	10.9	1,372	0.8	3.7	1.02	—
1969*	46,873	14.3	1,578	15.0	3.8	1.24	1.63
1970	39,748	(15.2)	1,834	16.2	3.9	1.24	1.64
1971	42,822	7.7	1,453	(20.8)	3.7	1.25	1.63
1972*	53,170	24.2	1,137	(21.7)	2.7***	—	2.19
1973	52,753	(0.8)	1,119	(1.6)	2.1	—	2.49
1974	55,676	5.5	1,069	(4.5)	2.0	—	2.63
1975	57,577	3.4	1,195	11.8	2.1	—	2.73
1976**	55,600	(3.4)	1,035	(13.4)	1.8	—	2.51

* Section B—Accident Benefits Coverage—optional, effective January 1, 1969; mandatory for liability insurance purchasers, effective January 1, 1972.

** Limitation for filing action was one year, extended to 2 years, July 1976.

*** Drop in Ratio

Sources: Ministry of the Attorney General, Ministry of Transportation and Communications, Insurance Bureau of Canada

- Initial payments for losses have been provided at a much earlier date than under a full fault system (Massachusetts and Florida). In Massachusetts 63.3 percent of no-fault claimants received their first payments within 90 days.
- Automobile negligence cases filed before the courts have shown a measureable decline (Massachusetts, Florida, Michigan).
- Attorney representation in handling small claims has declined markedly (Massachusetts and Florida). It should be noted that both these states had very high levels of attorney representation under the prior tort system.
- The aggregate cost of insurance has been reduced (Michigan) and the ratio of benefits to premiums has increased (Florida).
- The number of non-serious and nuisance claims has declined under the first-party system (Massachusetts and Florida).
- Claimants are completely satisfied, in the majority of cases, with the indemnity received (Massachusetts and Florida).
- A majority of economic losses are being covered entirely by the first-party payments. 40% of claims in 1971 in Florida were for first-party payments; in 1973, 70% were first-party claims. No more than 5% of first-party claimants in a Massachusetts study of no-fault had incurred economic losses in excess of the Personal Injury Protection coverage limit of \$2,000.

The U.S. Department of Transportation completed in June 1977 a 16-state survey of no-fault automobile insurance programs.¹ The report concludes that “no-fault automobile insurance works”.

It reviewed the findings in Massachusetts, Florida and Michigan and reported additional findings:

- In states with unlimited first-party medical benefits, such as Michigan, New Jersey and Pennsylvania, unprecedented levels of compensation are being provided to grievously injured accident victims . . . Seriously injured victims in at least these three states have a better chance of recovering their economic loss under the no-fault system.
- While data on coordination of no-fault benefits with other insurance coverage are sparse, significant premium savings appear to be available where benefit coordination is possible.
- The major shift to first-party benefits documented for the no-fault states has undoubtedly significantly improved the cost efficiency of their auto insurance systems (chiefly in the relative reduction in claims personnel); the major unanswered question is the extent of this improvement.
- The observed improvement in timeliness and adequacy of payments clearly provides positive incentives for rehabilitation.
- Benefit maximizing no-fault plans must be accompanied by strong cost savings features if insurance prices are to be held in check . . . The expe-

1. U.S. Department of Transportation, *State No-Fault Automobile Insurance Experience, 1971-1977*, Washington, June 1977.

rience of the states, taken overall, does indicate that increased benefits under no-fault can be achieved through improved cost-efficiency and that no-fault does not necessarily mean higher insurance premiums, once inflation and other factors are taken into consideration.

In summary the study concludes that "State experience with no-fault automobile insurance would appear to confirm the basic soundness of the theory and the feasibility of the theory's implementation".¹ However, the report notes that most state no-fault plans have been "quite modest, both in terms of benefit levels and degree of restriction on tort liability".² Only the Michigan plan approaches the kind of comprehensive reform advocated by no-fault supporters.

As in Ontario, no recent studies in the U.S. no-fault states have been carried out to determine empirically whether significant further improvements in compensation can be effected by extending no-fault to cover larger losses, or by introducing a pure no-fault system.

5. Weaknesses of a Mixed Fault/No-Fault Approach

While advantages exist in introducing a partial no-fault system of compensation, this approach to reparations is by its nature a compromise that admits the failures of the fault system and yet does not meet the full objectives of the pure no-fault system. The mixed fault/no-fault approach to compensation has been criticized because it is said to hide certain shortcomings of the fault system without eliminating them. In particular, the 1977 Department of Transportation study in the United States pointed out that most existing no-fault plans in the United States:

"reflect not the no-fault advocate's conception of a sound and effective accident reparation plan but rather imperfect compromises wrought through the political process that in some cases have not only failed to realize the goals of reform but have actually created some new problems or aggravated old ones".³

Nevertheless, the mixed fault/no-fault approach need not be an "imperfect" or unsound solution to compensation, despite the inherent weaknesses of compromise. However, if the compromise approach is to be an effective plan, attention must be paid to the possible disadvantages of various compromise alternatives in order to assess the extent of their impact on the adequacy of compensation. Potential weaknesses are related to two factors:

1. the amount of compensation provided on a first-party basis; and
2. the existence and nature of the threshold to tort.

1. U.S. Department of Transportation, *op. cit.*, 1977, page 82.

2. *Ibid.*, page 77.

3. *Ibid.*, page 77.

Level of First-Party Benefits

The tort system has frequently been accused of failure to compensate the seriously injured person adequately and promptly. A limited plan of no-fault benefits, retaining the right to tort for a major portion of recovery, is similarly criticized because it does little to resolve this problem. It is considered to be inadequate because:

- A limited plan of no-fault benefits concentrates on transferring minor claims to the more efficient first-party system of compensation. Major claims, which experience the greatest problems of delay and cost under the tort system, still must often rely on extended procedures of fault investigation and legal action to obtain full compensation.
- The seriously injured person must still seek compensation under the fault system, because no-fault benefits are not designed to fully indemnify him for his economic losses. However, he is not assured of any further recovery under the tort system. In particular, the seriously injured victim, who is held to be either fully or partially responsible for his injury, is not guaranteed any extra indemnity to support himself or his family.
- No-fault benefits can be used by the claimant to “finance” long negotiations, prolonging settlement of claims in hopes of higher awards. Use of no-fault benefits in this manner contributes to higher costs both for the insurer and the claimant, and can retard rehabilitation.
- As the level of benefits increases on a first-party basis, the excess loss for which there is recourse to the courts decreases. Therefore the eventual liability of the negligent party diminishes. As a result, voluntary purchase of liability insurance at high limits to cover serious injury becomes less attractive, because of the minimal risk of reimbursing large losses on a third-party basis.

A threshold to tort is designed to eliminate recovery of non-economic loss in minor claims. The limits set for tort recovery can be entirely arbitrary: therefore one class of victim recovers for pain and suffering; another class does not. The arbitrary nature of the threshold to tort is easily subject to criticism, whether the threshold is based on a dollar limit or on a definition of serious injury. Specific criticisms include:

- Any dollar threshold becomes progressively more meaningless during any inflationary period.
- A dollar threshold based on medical costs becomes a target for the less seriously injured. It encourages overutilization of first-party benefits in order to reach the threshold permitting recovery from the third-party insurer.
- Any threshold to tort makes every case involving more than superficial injuries a potential lawsuit to be investigated by the liability insurer.
- A verbal threshold limiting tort recovery to cases of serious injury re-

quires that the injured party test the threshold to determine whether his injury qualifies for tort recovery. This procedure involves delay, uncertainty, and legal expense. It adds another element of chance to the already existing uncertainties of the tort system.

- An effective threshold to tort will curtail the number of claims that require legal counsel and may discourage general legal practitioners from qualifying in this area of litigation. As a result, the victim may experience difficulty in finding expert legal help, or undue delays before his case can be taken on by the few remaining legal specialists.
- A verbal threshold limiting recovery of non-economic loss to those that are seriously injured or significantly disfigured discriminates against the majority of persons with lesser injuries who suffer inconvenience and pain without similar compensation. It is inconsistent with the no-fault concept because it treats different classes of individuals differently. It is also inconsistent with the fault concept, because it removes liability or responsibility from the driver causing minor injury, but retains the responsibility principle for the driver who causes serious injury, even when there is little difference in the degree of negligence.

Treatment of the seriously injured victim is ultimately the basis for many of the criticisms cited above. The problems and inequities of the tort system are most apparent in the compensation of the seriously injured, and pure no-fault supporters argue that a mixed approach does not resolve these problems. On the other hand, supporters of the tort system argue that, without tort recovery, full recovery of losses is denied.

6. Summary

In summary, the supporters of the fault system defend tort recovery over no-fault recovery for the following reasons:

- It guarantees recovery foremost to the innocent victim.
- It compensates for intangible loss.
- It provides an adaptable and individualized mechanism for evaluating damages.
- It provides an impartial, "well-tried" mechanism for settling disputes.
- It encourages responsibility.

Yet some supporters of the fault system are willing to sacrifice these advantages in the case of claims resulting from minor injury. They recognize the need to extend some level of benefits to all victims of automobile accidents and they recognize the potential for savings when claims are shifted to a first-party mode of recovery. In order to effect this reform without an unacceptable increase in insurance costs, they are willing to limit tort rights for persons with minor injuries.

However, they maintain that a pure no-fault system is second-best in certain respects, particularly in its approach to intangible loss, and thus

TABLE 5
ISSUES AND APPROACHES TO NO-FAULT

Issues	Decisions	Consequences	Pure Fault	Mixed Fault/ No-Fault	Pure No-Fault
Distribution of Liability Based on Negligence	Yes	Tort System		Above Threshold	
	No	First-Party Payment		Partial	
Only The Innocent Recover	Yes	Tort System		Above Threshold	
	No	No-Fault Benefits		Partial	
Right to Evaluation of Damages by Courts Based on Individual Consideration	Yes	Reintroduce Fault and Tort System		Above Threshold	
	No	Schedule of Indemnities		Partial	
Compensation for Intangible Loss	Yes	Case-by-Case		Above Threshold	Unlikely
		Schedule		Below Threshold	Alternative
	No	No Recovery			
Recourse to Courts for Settlement of Disputes	Yes	Tort System		Above Threshold	
		Contractual Disputes		Alternative	Alternative
	No	Non-Adversary Appeal Procedure			

should not be the sole means of compensation for the seriously or permanently injured. It is strongly argued that the public conscience calls for individual consideration to be given to evaluating the losses of the seriously injured. Hence the need for a compromise solution to compensation that combines both fault and no-fault advantages.

The depth of reform within the compromise solution can vary greatly. Some reforms suggest little more than patching on a limited package of first-party benefits, leaving the fault system virtually intact. Others essentially adopt a full first-party approach to compensation for economic loss, patching on tort rights for the seriously injured.

Each is still a compromise to the pure no-fault principle of treating all victims according to the same standards. The first preserves the fault concept, and its discrimination between guilty and innocent, conceding only that *some* protection for bodily injury is required by all victims. The second largely denies the fault concept and the right to recovery for intangible loss but reintroduces both for a particular class of victim.

The major issues and choices in the fault/no-fault dilemma are summarized in Table 5 above and expanded into the questions that follow:

— Should some compensation be provided to all automobile accident victims?

- Is the fault concept worthy of preservation in the automobile reparations system?
- Does a no-fault approach offer an acceptable substitute system of compensation for economic loss? Will the claimant be satisfied that he has been adequately compensated?
- Does the public demand that intangible loss be compensated in any substitute system?
- Does the public demand a case-by-case evaluation of intangible losses?
- Is the public ready to sacrifice individualized evaluation of intangible damages in the majority of minor claims, in order to effect reforms in compensation for economic loss?
- Will the public demand recourse to the courts to settle claim disputes?

Answers to these questions will determine to some extent the approach to be favoured in reforms to the automobile accident compensation system. If the answers point to a compromise solution that mixes first-party benefits with some recourse to tort action, then the depth of reform with regard to the degree of tort restriction must also be considered.

G. THE COST CONSEQUENCES OF NO-FAULT

The issue of the cost of no-fault automobile insurance is divided into two separate elements. The first element is one of cost *efficiency*. If no-fault proposals are to compete as effective substitute methods of compensation, they must demonstrate to the owner of an automobile that they make efficient use of his premium dollar, by cutting down the costs of delivering benefits.

The second element is one of *total* costs. If no-fault proposals are to remain affordable to the premium payor, reform of the reparations system must take into account not only the level of benefits that meets the major needs of the benefit recipient, but also the total revenues required to support that level of benefits.

This section addresses itself to both these issues, by considering the relative differences in each element of cost among three approaches to no-fault insurance:

1. a *pure* no-fault plan;
2. a *mixed* fault/no-fault plan, with a threshold to tort, barring recovery of non-economic loss except in cases of severe injury;
3. a scheme of *enriched* first-party benefits, with no restriction to tort for non-economic loss and residual economic loss.

The following discussion concentrates on compensation for bodily injury. Section I examines the cost consequences of no-fault insurance for property damage. As background for later discussion, current data on benefit costs and claims expenses in Ontario are presented below.

TABLE 6
BENEFITS PAID IN ACCIDENTS INVOLVING PRIVATE PASSENGER VEHICLES
1975 Policy Year As At December 31, 1976

Coverage	Losses and Loss Adjustment Expenses Incurred (\$)	Number of Claims	Average Cost Per Claim (\$)	Cars Insured	Loss Costs Per Car Insured (\$)
Bodily Injury					
a) Accident Benefits					
Medical-Funeral	4,844,527				
Weekly Disability	17,593,282				
Death Benefits	3,059,701				
Total	25,497,510	35,060	727	2,731,944	9.33
b) Third-Party Liability					
Bodily Injury	155,692,662	28,038	5,553	2,748,782	56.62
<i>Bodily Injury Total</i>	181,190,172	63,098	2,872	2,740,363*	66.12*
Property Damage					
a) Vehicle Damage					
Collision and All Perils	117,483,995	179,938	653	2,074,437	56.63
Comprehensive and Specified Perils	34,678,506	163,694	212	2,475,178	14.01
Total	152,162,501	343,632	443	...	
b) Third-Party Liability					
Property Damage	120,686,326	189,726	636	2,748,782	43.91
<i>Property Damage Total</i>	272,848,827	533,358	512	...	114.55 ¹
GRAND TOTAL ALL COVERAGES	454,038,999	596,456	761	...	180.67 ²

* Average

1. For insured covered for Collision, Comprehensive and Third-party Liability (property damage component only)

2. For insured covered for Collision, Comprehensive Third-party Liability and Accident Benefits

Source: Insurance Bureau of Canada, *1976 Automobile Insurance Experience*. (Green Book)

1. Costs of the Current Ontario System of Reparations for Automobile Accident Losses

Distribution of Benefit Costs in Ontario

Roughly 60% of benefits paid out by the automobile insurance industry in Ontario are for property damage settlements, and 40% for bodily injury. Table 6 above and summary Table 7 below illustrate claims experience for 1975 in accidents involving passenger vehicles.

Over 80% of bodily injury benefits are distributed through third-party settlements, while less than half of property damage payments fall under third-party modes of payment.

Noteworthy is the difference in the average size of bodily injury claims paid on a first-party and third-party basis. Table 6 shows that third-party benefits are on average eight times larger than current "no-fault" payments. In contrast, the size of settlement in the property damage area varies little between modes of payment and is therefore not an issue in the fault/no-fault debate.

TABLE 7
BENEFITS PAID IN ACCIDENTS INVOLVING
PRIVATE PASSENGER VEHICLES 1975 POLICY YEAR

	Benefits Paid (\$ Million)	Percent of Total
<i>Bodily Injury</i>		
Accident Benefits	\$ 25	6%
Third-Party Liability	156	34
	\$181	40
<i>Property Damage</i>		
Vehicle Damage (First-Party)	152	33
Third-Party Liability	121	27
	273	60
<i>Total Benefits Paid</i>	<u>\$454</u>	<u>100%</u>

Source: Table 6

Assuming that the average third-party claim of about \$5,500 for bodily injury represents a measure of complete recovery under the tort system, elimination of tort rights requires that the substitute compensation system, ideally, match this "full" recovery figure. However, if the new system opens up compensation to all accident victims and not just the "innocent", the average "full" recovery claim of the tort system cannot be matched without increased premium cost. Somewhere a trade-off in benefits is necessary: commonly, a trade-off is suggested in the area of non-economic loss.

Distribution of Claims Expenses in Ontario

For each dollar of benefits paid by insurers in Ontario, roughly 63 cents must be spent in insurance company expenses and claims adjusting costs. Table 8 on the opposite page demonstrates the breakdown of expenses, based on average annual costs during the 1971 to 1975 period. Estimates of claims adjusting expenses are based on periodic analyses conducted by the industry. Information concerning expenses in specific areas, such as bodily injury, property damage, first-party and third-party claims is not reported separately, so no conclusions can be drawn on industry performance within specific categories of loss.

Over the 1971 to 1975 period, premiums earned fell below the total expenditures required for delivery of benefits. Although 66 cents of each premium dollar earned is returned to the claimant, Table 8 also shows that 42 cents is used to cover claims handling and other expenses, causing a shortfall in underwriting revenue. The insurance industry has been able to support this deficit through the addition of investment and other income which form an integral part of its revenue base.

It is the aim of the pure no-fault system to contain premium costs. It can do so in two ways: by reducing the 66 cents of each premium dollar paid out in benefits, or by reducing the 42 cents used to cover claims handling and other expenses. Most no-fault proposals seek to distribute the 66 cents

of benefits towards higher economic loss payments rather than reduce the total value of benefits paid from the insurance pool. Instead, they aim to achieve savings in the 42 cents now going to claims handling and other expenses by substituting a first-party system of recovery. This reduction in total expenditures required to deliver benefits can be used to lower premiums or to increase payments under current premiums to an amount greater than 66 cents. The potential for cost efficiency under no-fault is considered below and applied to Ontario claims experience.

TABLE 8
 BREAKDOWN OF EXPENSES, ONTARIO AUTOMOBILE INSURANCE INDUSTRY 1971 to 1975

	Annual Average 1971-1975	Cost of Delivery of \$1.00 in Benefits	
Company Expenses			
Commissions	\$ 77,000,000	.21	
Premium Tax	11,000,000	.03	
General Expense	81,000,000	.22	
Claim Adjusting Expenses	61,000,000	.17	
Total Industry Expenses	230,000,000	.63	\$.42
Benefits to Claimants			
Excluding Adjusting Costs	365,000,000	1.00	.66
Total Expenditures	\$595,000,000	\$1.63	\$1.08
Premiums Earned	\$550,700,000	\$1.51	\$1.00
		Premium Cost To Policyholder of \$1.00 of Benefits	

Source: The Select Committee on Company Law, *First Report on Automobile Insurance*, page 190.

2. Improvements In Cost Efficiency Under No-Fault

Which costs are affected by a switch from tort recovery to no-fault recovery? The cost components of delivering benefits under the tort system are best illustrated by U.S. experience, where much of the impetus originated for a switch to no-fault automobile reparations. The U.S. experience also provides a point of reference for Canadian cost comparisons. Before the introduction of no-fault features into many states in the early 1970's, U.S. studies shown in Table 9 indicated that for every \$1.00 of benefits paid out to claimants for personal injury losses, 67 cents was retained for insurance company expenses and claims adjusting costs.

Legal and Court Costs

A dramatic increase in delivery costs occurred when the *net* benefit to the claimant was considered. Whereas the insurance industry spent 67 cents to distribute \$1.00 in benefits, 30 cents of the \$1.00 in benefits paid by the

**NET RECOVERY BY CLAIMANTS IN THE UNITED STATES IN PERSONAL
INJURY LIABILITY CLAIMS**

TABLE 9

	Distribution of Premium Dollar	Cost to Insurers of Delivering \$1.00 in Benefits
Premiums	\$1.00	
Company Expenses		
Selling	.18	\$.30
Overhead	.05	.08
State Taxes	.03	.05
Total Company Expenses	.26	.43
Claim Adjusting Expenses	.14	.23
Total Expenses	.40	.67 ←
Benefits Paid by Insurers	\$.60	\$1.00
Less Claimants' Legal Fees	.16	.27
Less Court Costs	.02	.03
<i>Net Benefits Received by Claimants</i>	<i>\$.42</i>	<i>\$.70</i>

industry went to lawyers' fees and court costs rather than into the claimant's pocket. The claimant's net recovery was 70 cents. The total dollar input in expense costs to obtain 70 cents in benefits was 97 cents. Therefore, as shown in Table 10, the claimant paid out an estimated \$2.38 in premiums to recover \$1.00 in *net* benefits.

This situation has changed in many U.S. states adopting "no-fault" features in their automobile insurance plans. Massachusetts, Florida and Michigan, for example, have been able to demonstrate a marked drop-off in litigation as a result of no-fault introduction.

The situation in Ontario is likewise not analagous to early 1970 experience in the United States. First, the extent of litigation in this Province is less than in many U.S. jurisdictions. For example, 79% of bodily injury

TABLE 10

	Distribution of Premium Dollar	Dollar Input by Claimant for \$1.00 in <i>Net</i> Benefits Received
Premiums	\$1.00	\$2.38 ←
Company Expenses	.26	.62
Claim Adjusting Expenses	.14	.33
Claimants' Legal Fees and Court Costs	.18	.43
Total Expenses, Fees, Costs	\$.58	\$1.38
<i>Net Benefits Received by Claimants</i>	<i>\$.42</i>	<i>\$1.00</i>

Source: U.S. Senate Antitrust and Monopoly Subcommittee, in Rokes, W.P., *No-Fault Insurance*, Insurers Press, Inc., Santa Monica, California, 1971, page 138.

cases in Massachusetts involved legal counsel prior to no-fault introduction. Studies in Quebec point out that close to 30% of injury claims involved legal counsel,¹ and a 1968 survey in British Columbia showed 20% legal involvement.² A similar survey has not been conducted recently in Ontario, but legal representation in this Province is considered by the industry to be well below the current 40% experience of the Motor Vehicle Accident Claims Fund in personal injury claims, and 25% experience for property damage claims.³

Secondly, contingent fees in the United States permit a higher ratio of legal fee to award-amount than in Ontario. Fees approaching one-third the recovery amount are common in the U.S. and sometimes reach 40% of the recovery when the case is tried. In Ontario, fees are considered to average 15% to 20% of the award amount.

Thirdly, most U.S. states in the late 1960's and early 1970's were still under "contributory" negligence laws, which barred claimants from recovery if they shared in the negligence causing an accident. As a result, high legal costs in the U.S. were borne by a large number of unsuccessful claimants. Later, at the time that no-fault plans were made compulsory, many states introduced legislation to allow "comparative" negligence rulings, permitting partial recovery of damages, as in Ontario.

Finally, there were no compulsory no-fault plans in any of the states when the comprehensive U.S. study reported above was carried out in 1969-1970. Ontario today has a mandatory scheme of no-fault benefits, which has reduced reliance in this Province on the fault system for recovery of loss.

Net Recovery by Claimants

There is no reliable current information in Ontario to demonstrate the effect of legal fees and claims adjusting costs on the net benefits received by the claimant. However, based on data assembled for the Insurance Bureau of Canada *No-Fault Study* of 1974, carried out by the actuarial firm of Woodward and Fondiller, a rough comparison can be made of legal and claims adjusting costs between the U.S. study cited above and claims experience in four Canadian Provinces in a two month period in 1973. Ontario was one of the Provinces studied, together with Nova Scotia, New Brunswick and Alberta.

Canadian claimants appear to have received more in net benefits from their premium dollar than did their U.S. counterparts in the earlier U.S. study reported by the Senate Subcommittee. Tables 11 and 12 illustrate the

1. Government of Quebec, *Report of the Committee of Inquiry on Automobile Insurance*, March 1974, Table 4, page 197.
2. Province of British Columbia, *Royal Commission on Automobile Insurance*, Report of the Commissioners, July 30, 1968, Table 2.1, page 99, Volume 1.
3. Woods, Gordon & Co., "Processing of claims by the Insurance Industry", *Report IV* to the Select Committee on Company Law, March 1977, page 10.

**NET RECOVERY BY CLAIMANTS
PERSONAL INJURY LIABILITY CLAIMS**

TABLE 11

	Costs to Insurers of Delivering \$1.00 in Benefits	
	U.S. Experience 1969	Canadian Experience (Four Provinces) 1973
Company Expenses	\$.43	\$.46
Claim Adjusting Costs	.23	.13 ¹
Total Expenses	<u>.67</u>	<u>.59</u>
Benefits Paid by Insurers	\$1.00	\$1.00
Less Legal and Court Costs	.30	.16
<i>Net Benefits Received by Claimants</i>	<u>\$.70</u>	<u>\$.84</u>

TABLE 12

	Dollar Input by Claimant for \$1.00 in Net Benefits Received	
	U.S. Experience 1969	Canadian Experience (Four Provinces) 1973
Premiums	<u>\$2.38</u>	<u>\$1.89</u>
	U.S. Experience 1969	Canadian Experience (Four Provinces) 1973
Company Expenses	.62	.55
Claim Adjusting Costs	.33	.15 ¹
Claimants' Legal and Court Costs	.43	.19
Total Expenses, Fees, Costs	<u>\$1.38</u>	<u>\$.89</u>
<i>Net Benefits Received by Claimants</i>	<u>\$1.00</u>	<u>\$1.00</u>

1. Excluding staff adjusters.

Source: U.S. Senate Antitrust and Monopoly Subcommittee, *Op. Cit.*

Woodward and Fondiller, *No-Fault Study*, Insurance Bureau of Canada, June 5th, 1974.

breakdown of costs associated with personal injury liability claims. In the Canadian example it is assumed that company expenses account for the same proportion of benefits as shown in Table 8 for all coverages in Ontario. All other Canadian ratios are taken from the Woodward and Fondiller study, and are derived in Appendix C. Biasing Canadian claims expenses downward is the exclusion of the cost of staff adjusters in claims adjusting expenses, although costs of independent adjusters are included.

Taking into account this bias and other assumptions, it still appears that the premium burden for net recovery of benefits in the four Provinces including Ontario is roughly 20-25% less than in the U.S. study cited: \$1.89 in the Canadian study compared to \$2.38 in the U.S. study. A major factor in this difference is the size of the plaintiff's legal and court costs. Whereas legal and court costs accounted for 30% of the benefits paid by insurers in the U.S., they accounted for only 16% in the Canadian study.

Complete elimination of legal costs from benefit payments in the American example could potentially reduce premium costs from \$2.38 to \$1.67 or about 30%. In the Canadian Provinces, the comparable saving would be about 10%, a decrease in premiums from \$1.89 to \$1.70 for the same \$1.00 level of benefits.

Therefore, the savings in benefit delivery costs to be derived from elimination of legal expenses in the Canadian context will not be as great as was advocated by no-fault proponents in the United States. However, when the 16% ratio of legal expenses to benefits paid by insurers, is applied to Ontario third-party loss experience in bodily injury claims, elimination of plaintiff legal and court costs releases significant sums, estimated at roughly \$20 million in 1975, that become available to increase benefits or contain premiums.

The total savings predicted above would occur only under a pure no-fault plan. A mixed fault/no-fault approach would eliminate some of the legal expenses from claimant award amounts, but the potential for savings would be less. Further savings can be achieved through a no-fault approach in the categories of company and claims adjusting expenses.

Cost of Delivering Benefits Under Different Types of No-Fault Proposals

What is the extent of savings in the delivery of benefits under an extended first-party system of compensation? Once again, using bodily injury data from the Woodward and Fondiller Study, illustrative estimates can be derived of the relative savings in both legal and adjusting expenses possible under three fundamentally different approaches to no-fault. These estimates are based on broad assumptions that distinguish the three approaches under consideration and are illustrated in Tables 13 and 14.

A pure no-fault plan completely eliminates claimants' legal costs and significantly reduces adjusting expenses. Its total cost for delivery of \$1.00 of net benefits to the claimant is \$1.52, a saving from the \$1.89 cost under the liability system. A mixed fault/no-fault plan, with a threshold to tort based on a definition of serious injury, requires \$1.73 to be spent to provide \$1.00 in net benefits, thereby producing only an 8% saving in overall delivery costs. Finally, a plan of enriched first-party benefits, with no restriction to tort recovery of non-economic loss, results in the smallest savings over

**COMPARISON OF COSTS OF DELIVERING NET
BENEFITS UNDER VARYING APPROACHES
TO NO-FAULT—CANADIAN EXPERIENCE**

TABLE 13

Costs to Insurers of Delivering \$1.00 in Personal Injury Benefits				
	Liability Claims, 1973	Pure No-Fault	Mixed Fault/No-Fault	Enriched Benefit Scheme
Company Expenses	\$.46*	\$.46*	\$.46*	\$.46*
Claim Adjusting Costs	.13	.06	.09	.11
Total Expenses	.59	.52	.55	.57
Benefits Paid by Insurers	\$1.00	\$1.00	\$1.00	\$1.00
Less Legal and Court Costs	.16	—	.12	.12
<i>Net Benefits Received by Claimants</i>	<u>\$.84</u>	<u>\$1.00</u>	<u>\$.88</u>	<u>\$.88</u>

TABLE 14

**Dollar Input by Claimant for \$1.00 in Net Personal
Injury Benefits Received**

	Liability Claims, 1973	Pure No-Fault	Mixed Fault/No-Fault	Enriched Benefit Scheme
Premium	<u>\$1.89</u>	<u>\$1.52</u>	<u>\$1.73</u>	<u>\$1.76</u>
Company Expenses	.55	.46	.52	.52
Claim Adjusting Costs	.15	.06	.10	.13
Claimants' Legal and Court Costs	.19	—	.11	.11
Total Expenses, Fees, Costs	\$.89	\$.52	\$.73	\$.76
<i>Net Benefits Received by Claimants</i>	<u>\$1.00</u>	<u>\$1.00</u>	<u>\$1.00</u>	<u>\$1.00</u>

* Assumed constant, based on Table 8.

Source: Estimates based on Woodward and Fondiller, *op. cit.* See also Appendix C.

the current method of compensation since \$1.76 must be spent to deliver \$1.00 in net benefits.

The greater savings of the pure no-fault plan result from elimination of legal expenses paid by insurers on behalf of claimants, and from reduction in internal legal expenses associated with claims adjustment. Other costs of adjusting are estimated by the I.B.C. study to increase by 40% to indicate greater reliance on staff adjusters. However, the overall expense of claims adjustment is significantly reduced.

Smaller savings in mixed approaches to no-fault occur as a result of continuing legal involvement in certain claims. In the enriched benefit approach, legal expenses are assumed to be reduced by only 25%, as 75% of third-party awards are for general damages that will continue to involve legal advice if there is no restriction of tort action.

Derivation of these estimates is described in Appendix C. Company expenses are assumed to be constant under all three approaches to no-fault. The available data do not permit a reliable estimate to be made of the effect of reorganization to first-party modes of payment on the general and selling costs of the insurance company.

It should be noted that there are other methods of lowering benefit delivery costs and increasing the return on the premium dollar that are unrelated to no-fault. Reduced costs through greater company efficiency could have a significant impact on delivery costs. For example, strong competition among insurance companies can stimulate administrative efficiency. Marketing advantages of a government corporation or monopoly could create other cost reductions, bringing higher benefit return at lower cost. The issue of a government corporation in the automobile insurance market is discussed elsewhere in the Committee's Second Report on Automobile Insurance.

In conclusion, there *are* cost efficiencies that can be obtained in the delivery of accident benefits in Canada and in Ontario through extension of no-fault. They do not appear to be as great as those initially estimated by proponents of no-fault in the United States in the early 1970's. But because of the size of the industry in this Province even small fractional savings can result in significant dollar savings to the Ontario system of automobile insurance.

Cost efficiencies in the delivery of benefits under no-fault will depend largely on savings to be achieved in claims adjusting expenses, by elimination of third-party bargaining procedures; and in legal expenses, by elimination of the need for legal counsel and for litigation of claims. General administrative expenses may change through reorganization of claims handling, but the direction or extent of change is difficult to predict without an evaluation of specific procedural changes.

The most significant reduction in the cost of delivering benefits would be achieved through a pure no-fault approach to compensation.

3. Redistribution of Total Benefit Costs Under a No-Fault System of Reparations

Can bodily injury benefits be shifted to first-party payments without increasing total costs? When compensation for bodily injury is shifted away from the fault system to first-party modes of payment under no-fault plans, the population of injured persons receiving benefits expands. Under the pure fault system, only "innocent" victims recover. Under a no-fault system, potentially every injured person will recover his losses *to some degree*. New claimants will necessarily create higher total costs, unless the average cost of each claim is limited below the level of full tort recovery.

The largest single class of victims added to the reparations system under no-fault is the driver injured in a single-car accident. 25% of persons

injured in Ontario automobile accidents receive their injuries in single-car accidents.¹ Since 1972, most are eligible for limited compensation under Accident Benefits coverage, but not for full recovery under the liability system.

In contrast, in the United States before interest in no-fault developed, the driver in a single-car accident rarely recovered under the tort system. When no-fault was introduced in many states, this class of injured person added substantially to no-fault loss costs. Studies in Massachusetts indicated that total loss costs appeared to grow in proportion to the number of single-car accidents brought under the no-fault plan.

Therefore, in the present Ontario situation, where Accident Benefits coverage is mandatory for liability policy holders, a shift to further no-fault benefits should not introduce any large new class of recipients. Those drivers not now insured under liability coverage (about 7-12%), and possibly those excluded from receiving Accident Benefits by reason of breach of condition would be the only new class of insured person eligible for first-party recovery. In 1976, 4% of accidents in Ontario involved an "impaired" driver; another 9% involved a driver who "had been drinking" and who may or may not have been excluded from Accident Benefits.² Instead, the major thrust of a further shift to no-fault in Ontario would be the redistribution of funds away from losses under liability coverage towards losses under no-fault coverage.

The cost consequences of three possible adjustments to the level of first-party or accident benefit payments are illustrated in Tables 15, 16 and 17. Identical adjustments that enrich first-party benefits are shown under three different types of "no-fault" proposals:

1. a *pure* no-fault plan;
2. a *mixed* fault/no-fault plan with a threshold to tort, barring recovery of non-economic loss, except in the case of serious injury;
3. a scheme of *enriched* first-party benefits, with no restriction to tort for non-economic loss and residual economic loss.

An attempt is made to derive "reasonable" estimates of cost shifts caused by extension of no-fault features into the Ontario claims situation. However, *the amounts calculated are intended to be more illustrative than actual*. The data required to permit estimation of all anticipated cost factors are generally not available. In order to fully evaluate cost shifts caused by a no-fault plan for bodily injury, if such a plan is approved in principle, would require detailed data concerning:

1. Ontario Ministry of Transportation and Communication, "Motor Vehicle Accident Facts, 1976".
2. Ontario Ministry of Transportation and Communication, "Motor Vehicle Accident Facts, 1976".

- the economic status of the people injured,
- injuries by type,
- disability periods,
- medical and hospital costs of injury,
- dependency status of the injured's family, and other similar factors.

The insurance industry does not collect these data on a regular basis, as the majority of losses are paid to unknown third parties who cannot be identified for the purposes of setting premiums. Hence industry statistics concentrate on losses incurred rather than on who incurs these losses. A detailed claims study is required to produce a profile of the claimant and his need for indemnity.

Under each of the three alternative plans, the total amount spent by the insurance industry to cover personal injury losses in 1975 is kept constant at \$182 million, thereby maintaining premium rates at a constant level. The examples shown in Tables 15, 16 and 17 illustrate the amounts that must be freed up from liability coverage in order to cover the higher first-party costs of the three proposed increases in no-fault benefits coverage.

No allowance is made for a transitional stage of adjustments to no-fault. Costs are estimated in Appendix C for a typical loss year, similar to 1975 experience. No provision is made for differences in claims settlement costs between first-party and third-party methods of recovery. As the following analysis is primarily for illustrative purposes, no provision has been made for the recent announcement of the government that amounts payable under Accident Benefits coverage would be increased effective July 1, 1978. Furthermore, data do not exist to permit the following analysis to be based on the new level of benefits. It should be noted, however, that the adjustment made by the government in increasing Accident Benefits coverage falls within the definition of an "add-on" or enriched benefit approach to no-fault, as described later in this section with reference to Table 17. The first-party benefit enrichments used in the examples are as follows:

A. quadrupling of the wage loss limit

The current maximum allowable wage loss benefit in Ontario is \$70 per week.* Quadrupling of the wage loss limit raises the maximum allowable indemnity to \$280 per week. The two-year limitation for benefit payments is retained. Net recovery is based at 85% of actual wage loss, up to the maximum limit.

It is expected that, with a limit set at \$280 per week, the average recipient will recover a wage loss at a level corresponding to the average wage in the Province—in mid 1977, \$252 per week. On a net basis this would amount to about \$215 per week, three times the present maximum

* Effective July 1, 1978, the maximum payable for loss of earnings doubles to \$140 per week.

ILLUSTRATIVE EXAMPLE
BODILY INJURY CLAIMS
UNDER THREE TYPES OF "NO-FAULT" SYSTEMS

TABLE 15

PURE NO-FAULT

	1975 Losses Passenger Vehicles \$ Million	Quadruple Wage Loss Limit (A)	Permanent Disability (B)	Earnings Related Death Benefits (C)
<u>Accident Benefits</u>				
Medical/Funeral	\$ 5	\$ 5	\$ 5	\$ 5
Weekly Indemnity	18	65	84	84
Death Benefits	3	3	3	37
Total	26	73	92	126
<u>Third-Party Liability</u>	156	109	90	56
<u>Total Losses</u>	<u>\$182</u>	<u>\$182</u>	<u>\$182</u>	<u>\$182</u>

TABLE 16

MIXED FAULT/NO-FAULT

<u>Accident Benefits</u>				
Medical/Funeral	\$ 5	\$ 5	\$ 5	\$ 5
Weekly Indemnity	18	65	84	84
Death Benefits	3	3	3	37
Total	26	73	92	126
<u>Third-Party Liability</u>				
Minor Injury	106	59	40	6
Serious Injury	50	50	50	50
Total	156	109	90	56
<u>Total Losses</u>	<u>\$182</u>	<u>\$182</u>	<u>\$182</u>	<u>\$182</u>

TABLE 17

ENRICHED BENEFITS

<u>Accident Benefits</u>				
Medical/Funeral	\$ 5	\$ 5	\$ 5	\$ 5
Weekly Indemnity	18	65	84	84
Death Benefits	3	3	3	37
Total	26	73	92	126
<u>Third-Party Liability</u>				
Amount Required to Maintain Total Recovery at Current Level	156	132	119	96
<u>New Costs</u>				
Not Freed from Liability Claims	-	(23)	(29)	(40)
<u>Total Losses</u>	<u>\$182</u>	<u>\$182</u>	<u>\$182</u>	<u>\$182</u>

AMOUNT FREED (NOT FREED) TO THIRD PARTY BENEFITS

FOR ILLUSTRATIVE PURPOSES ONLY

- a Data are not available to permit estimation of all anticipated cost factors.
 a A detailed claims study must be undertaken to derive more reliable cost estimates.

Source:

See Appendix C.

recovery of \$70 per week. Loss costs under this adjustment in first-party benefits are therefore expected to increase threefold, from \$18 million to \$54 million.

It is important to note that no provision is made to estimate the additional first-party cost of making the automobile insurance system first-payor. Under the present system in Ontario, the automobile insurer pays full wage loss indemnity up to \$70 per week for the first two weeks. After the second week, payments from the automobile insurer are frequently made on a pro-rata basis with other wage continuation plans.

If the automobile insurance system is made first-payor, the present level of losses for weekly indemnity would be well above the current \$18 million. Quadrupling of the wage loss limit on this basis would impose a much greater cost on first-party benefits than indicated in this example. There is, however, no available experience-related basis for estimating the additional cost. To reiterate, no provision has been made for this factor in the cost examples of this section.

In order to allow for possible changes in claims frequency under improved first-party wage loss benefits, it is assumed that the number of claims increases by 20%. Total loss costs are therefore estimated to increase by \$11 million to \$65 million. The twenty percent increase estimate corresponds roughly to the percentage of persons presently not covered for Accident Benefits, either because the vehicle owner is uninsured (on average 10% of owners); or because they are ineligible for various reasons such as impaired driving (4-13% of drivers).

No allowance is made for weekly indemnity payments to persons who are not wage-earners, for example, students, the unemployed or homemaker spouses.

B. provision for permanent disability

In cases of permanent disability, as determined after a review at the end of two years, the period of entitlement to income replacement is made unlimited. Maximum allowable wage loss benefits are set at \$280 per week, gross.

The present value of continuous payments of wage loss to the permanently disabled is estimated at \$19 million per year. This amount is added onto the \$65 million cost created by adjustment A.

C. provision for death-benefits on an earnings-related basis

Death-benefits are made earnings-related, rather than lump-sum. Benefits are continued for 4 years, at the wage loss limit in adjustment A.

The present value of earnings-related death benefits is estimated at \$36 million replacing the \$3 million currently provided under Accident Benefits.

If total claim costs are to remain constant at \$182 million, any increases in first-party benefits must be “financed” by funds freed from third-party coverage. A pure no-fault system frees all funds under the liability section. Mixed fault/no-fault plans free only a proportion of third-party funds, as the right to tort is retained for certain categories of loss. The effects of the three adjustments postulated above are described in more detail below within three basic types of “first-party” proposals.

Pure No-Fault—Table 15

Under pure no-fault, third-party liability is completely eliminated. All funds in this coverage component are freed and can be applied to increase benefits under the Accident Benefits component.

Each adjustment in the level of benefits under first-party coverage draws upon funds in the liability section. Quadrupling of wage loss limits reduces the amount available for further first-party adjustments to \$109 million, from \$156 million. After adjustment C, only \$56 million is left in the liability section.

This \$56 million is *unlikely to be fully available* after the three adjustments made in Table 15. As indicated under adjustment A, no provision has been made for the additional funds required if automobile insurance is made first-payor.

Whatever is left of the \$56 million will remain as a contingency fund for other increases in first-party loss costs. It can, for example, be used to provide limited payments for non-economic loss, which have been sacrificed by elimination of the tort system. Payments of this kind are made available under the New Zealand compensation plan outlined in Table 7 of Appendix A. Or it can be used to increase medical and funeral allowances or to cover unexpected costs, such as new claimants with different loss experience.

No-Fault with a Threshold to Tort—Table 16

Under this mixed fault/no-fault approach to compensation, third-party loss payments are limited to cases involving serious and permanent injury.

The Woodward and Fondiller study estimates that roughly one-third of the amount of prior liability claims will remain under the tort system, given a threshold to tort based on a definition of serious injury and given improvement in first-party benefits.

For purposes of this example, one-third of \$156 million or about \$50 million is assumed to represent the value of claims for serious injury remaining under the tort recovery system. It is assumed that introduction of in-

creased first-party benefits under adjustments A, B and C will not further reduce the value of these tort claims by any significant amount. Serious injury claims will continue to be paid under the fault component of the mixed system, such that the \$50 million is not available to fund increased Accident Benefits.

The \$106 million remaining in the liability section is taken to represent third-party claims for minor injury losses which do not meet the threshold for tort recovery. Under the mixed system described in this example, benefits in the case of minor injuries are paid on a first-party basis only. Accordingly, the \$106 million used by the tort system to pay both economic and non-economic losses in cases of minor injury is freed to fund higher economic loss payments on a first-party basis.

Because the mixed system frees a somewhat lower amount of funds than does the pure no-fault system, only \$6 million in excess monies remains after adjustment C to cover any undetermined first-party costs. It should be noted that the \$6 million could be expanded by the extent to which first-party payments might lower the value of tort claims for serious injury: as indicated above, this factor is not explicitly considered in this example. Conversely, the \$6 million that remains after adjustment C may not in fact be available since provision has not been made for all anticipated cost factors, as previously indicated with respect to adjustment A.

Critical to the availability of funds for first-party coverage is the effectiveness of the threshold in restricting third-party payments to the small population of the severely injured. Should there be a tendency for minor claims to bridge the tort threshold, third-party claims will exceed \$50 million and improvement of economic loss benefits on a no-fault basis may rapidly absorb whatever funds are freed from the liability section.

Enriched Accident Benefits—Table 17

No restriction is placed on tort recovery in this third proposal for losses above the amounts already paid by the enriched Accident Benefits plan. Payments for non-economic loss under third-party cover are expected to remain at the current level. Enriched Accident Benefits, represented by adjustments A, B, and C, must be funded either from reductions in third-party settlements for economic loss, or through an increase in total losses and hence by increased premiums.

In this example, it is assumed that two-thirds of improvements to first-party benefits replace payments presently made on a third-party basis. The other one-third of improved first-party benefits are paid to those persons "at fault" in an accident, and therefore ineligible for tort claims. The choice of a one-third to two-third division of costs is arbitrary but is based partly on the assumption that a majority of claimants under the present Ontario insurance system are eligible for some measure, if not 100 percent, of third-party recovery.

For example, in adjustment A, quadrupling of the wage loss limit increases loss costs from \$18 million to \$54 million, adding \$36 million in first-party costs, two-thirds of which (\$24 million) are assumed to lower third-party claims to \$132 million, and one-third of which is assumed to add new costs to the system of \$12 million. The \$11 million, or 20% increase in total costs under adjustment A to account for new claimants, is also considered to be a new cost to the system, bringing the total of new costs to \$23 million. The \$132 million remaining in the liability section is sufficient to compensate claimants at the same level afforded by the \$156 million under the current system, given that after adjustment A a greater part of the tort claimant's loss is met by Accident Benefits payments. The impact of adjustment A might, of course, be greater if consideration were given to automobile insurance as first payor.

The cost of adjustments B and C are divided on the basis of one-third for new costs and two-thirds for reduction of third-party claim costs. As a consequence of adjustments A, B and C, the requirement for liability funds to compensate tort claimants at their current level of recovery is reduced from \$156 million to \$96 million.

New costs accumulate as soon as any improvement is made in first-party indemnity levels. By adjustment C, new costs are estimated to total \$40 million. These new costs cannot be funded from the liability section unless some restriction is made on tort recovery; that is, unless recovery for some types of claims (for example, minor injury claims), or some categories of loss (for example, non-economic loss) is denied to the tort claimant.

The additional costs and premium burden of enriching Accident Benefits without restricting tort recovery may initially be acceptable to the motorist. For example, after adjustment A an estimated \$23 million in new costs is generated, roughly doubling present first-party costs of \$26 million. Accordingly, a premium increase to around \$32 per insured from the \$16 cost for 1975-1977 Accident Benefits coverage might be expected if all new costs had been properly accounted for. It is evident, however, that further adjustments or enrichments of Accident Benefits would, at some point, increase premium costs to an unacceptable level.

It is interesting to note that the recent adjustment made by the government to increase amounts payable under Accident Benefits coverage will have an effect similar to the adjustments considered in this example in that some new costs will be accumulated, resulting in an anticipated \$6 to \$10 increase in premiums for Accident Benefits coverage. To offset a small portion of this increase it is possible that third-party costs will decline to some extent to permit a modest reduction in premiums for liability coverage.

The Total Cost Requirements of Expanding First-Party Benefits

The cost consequences of pure no-fault and other no-fault proposals are only important if a consensus is reached that significant expansion of first-

party benefits is essential to compensate automobile accident victims equitably.

If first-party benefits are kept at low levels of indemnity, creating large residual losses, then the tort system must be retained to expedite recovery of these residual losses. The higher delivery costs of the tort system may be tolerated or steps may be taken to improve efficiency.

Given that expansion of first-party benefits is considered to be essential, then the cost data developed in Tables 13 through 17 show that this expansion cannot be undertaken without either a limitation on liability claim payments or a premium increase.

Funding problems result when a programme of enriching Accident Benefits is undertaken without any restriction to tort recovery. Increased premiums are necessary to extend compensation for economic loss to more injured persons, without denying claims for non-economic loss. If a premium increase is to be avoided, then some measure of recovery of non-economic loss must be sacrificed.

A mixed fault/no-fault plan, with tort recovery effectively restricted to cases of severe injury, can release substantial funds for first-party benefits. But the tort restriction must be capable of eliminating the bulk of minor third-party claims. In addition it must free payments made to the "innocent" for minor non-economic loss to fund increased economic loss benefits for all victims. But, if enrichment of first-party benefits beyond the levels shown in Table 16 is considered to be desirable, then the retention of tort rights for serious injury cases could still create a loss deficit, and the need for higher premiums.

A recent statement by an insurance industry executive before the U.S. Senate Committee studying a proposed National Standard for a No-Fault Accident Benefits Act has supported the view that enrichment of benefits in an "add-on" approach to no-fault will increase costs. To quote:

"The Chairman: Why not adopt add-on plans in which you get substantial first-party settlements, but there is no restrictions of the right to sue? What is your opinion on that?

Mr. Lesnik (Vice-President, Kemper Insurance Company): My opinion is that that would simply be superimposing another benefit system on top of the system we already have, and it would do little more than increase substantially the cost of insurance. We feel that a solution that increases the cost of insurance is not acceptable"¹

1. Hearings before the Committee on Commerce, Science, and Transportation, United States Senate, "Standards for No-Fault Motor Vehicle Accident Benefits Act", 95th Congress, First Session on S.1381, July 13, 15, 18 and 20, 1977, page 91.

It is evident that complete elimination of recovery of non-economic loss and of tort rights provides the greatest potential for expanding first-party benefits without premium increases. Not only does it release all funds originally used to fund claims for non-economic loss, but it also frees funds used to support the operation of the tort system of recovery. The illustrative example in Table 15 cannot be used to predict accurately how great an enrichment of first-party benefits is possible without unacceptable premium increases; rather, specific pure no-fault proposals must be evaluated on the basis of a comprehensive claims survey to derive reliable costs.

In general, two basic decisions determine the premium cost requirements of the automobile injury compensation system:

1. What level of first-party benefits is considered to be equitable?
2. Should some measure of tort recovery be retained, for example, to accommodate evaluation and distribution of non-economic loss payments?

Table 18 illustrates broadly the cost consequences of these two decisions combined.

In general, the above cost analysis is one of several factors to be taken into account in assessing the desirability of an expanded no-fault programme. For example, it is necessary to note that the cost analysis developed in this section does not take into account the "value" to the claimant of retaining the right to recover non-economic loss on an individualized basis, the right to court evaluation of damages, and the right to demand full recovery from the negligent party. The judgemental value placed on these "rights" may outweigh the cost efficiencies and the compensation principles of a pure no-fault system.

TABLE 18
TRADE-OFF BETWEEN FIRST-PARTY BENEFITS AND TORT RIGHTS

First Party Benefits	Tort Eliminated	Tort Restricted	No Tort Restriction
Low	Definite Premium Decrease	Possible Premium Decrease	Small Premium Change
Moderate	Possible Premium Decrease	No Premium Change	Premium Increase
High	No Premium Change	Possible Premium Increase	Definite Premium Increase

H. INITIATIVES TOWARDS NO-FAULT IN ONTARIO AND IN OTHER JURISDICTIONS

Developments in Ontario and in other jurisdictions with respect to the issue of no-fault are presented in this section. Following, is a consolidation of the detailed features of certain proposed and existing insurance schemes that have been brought to the Committee's attention during its recent hearings on automobile insurance.

It is intended that this discussion will provide a perspective concerning initiatives towards no-fault that have been taken in Ontario and outside the Province. Secondly, a detailed review of the categories of loss covered in a selection of alternative automobile insurance plans will demonstrate:

1. What types of coverages are considered to be basic to the compensation system envisaged by various automobile insurance reformers, and
2. What types of losses are compensated on a first-party basis, and to what level of indemnity.

A similar review for property damage is presented in Section I.

1. No-Fault Developments in Ontario

Extensive debate about alternative methods of compensating victims of automobile accidents developed in the 1960's and culminated in a number of reforms both in North America and in other common law jurisdictions.

In Ontario, as outlined in the First Report on Automobile Insurance, initiatives towards no-fault began in 1960. In that year, the Legislative Assembly's Select Committee on Automobile Insurance received representations on a proposed no-fault system from the All-Canada Insurance Association and from a committee of benchers of the Law Society of Upper Canada. In 1961 that Select Committee tabled an Interim Report recommending the adoption of a partial no-fault element in Ontario automobile insurance coverage.

The Osgoode Hall Study on *Compensation for Victims of Automobile Accidents*, 1965, later provided an empirical basis for disputing the adequacy of personal injury benefits under the tort system of compensation. It found that only 42.9 percent of those injured received any reparation under the tort liability system, and only 28.8 percent recovered all of their economic loss.

In 1969 the Insurance Act was amended in order to permit no-fault benefits coverage to be written as a part of automobile insurance and also to adopt the recommendation that had been made by the Select Committee. The amendment provided that it would be optional to the policyholder as to whether he would select this coverage or not. This amendment included the addition of Schedule E to the Act, setting out the full text of the Accident Benefits Section. In 1972 Section B—Accident Benefits Coverage—was enriched and became mandatory in all automobile insurance policies issued in Ontario that contained third-party liability coverage.

In the following year, 1973, the Ontario Law Reform Commission released a report that examined the tort system and its adequacy as a method of compensating motor vehicle accident victims. It recommended that "an in-

tegrated, more appropriate and more efficient system should . . . replace the tort action".¹

In addition, it recommended specific proposals for a substitute system of compensation which would be based on first-party insurance. Two major elements of this system were to be:

- reparation for all pecuniary losses made without regard to fault, and
- no compensation for non-pecuniary losses.

The O.L.R.C. proposal was criticized by the Advocates Society of Ontario and by others because of its total rejection of the fault concept.

In 1974 the Insurance Bureau of Canada presented its own concept for a new reparation system, developed by a special committee appointed to investigate various no-fault proposals. Variplan, the Vehicle Accident Recovery Insurance Plan, intends to provide:

- prescribed payments for economic loss on a first-party basis, with coverage to be compulsory;
- the right to sue for economic loss only to the extent that the loss is in excess of the prescribed payments;
- the right to sue for non-economic loss only in the event of:
 - death
 - serious permanent injury, which includes substantial disfigurement and severe and prolonged disability (continuous not less than 120 days).

This proposal for a mixed fault/no-fault approach to compensation is still outstanding; it is compared to other selected proposals later in this section.

In its First Report on Automobile Insurance in March 1977, the Select Committee on Company Law noted the significance of the no-fault concept, but decided not to make recommendations at that stage in its proceedings as to the desirability of adopting any fundamentally new no-fault programme in the Province. However the Committee did recommend that benefits under the Accident Benefits coverage currently provided in the standard automobile policy should be substantially improved, particularly in keeping with recent inflationary trends. As already indicated, the government adopted the Committee's recommendations with some minor changes and announced an increase in Accident Benefits coverage to be effective July 1, 1978.

2. No-Fault Developments Elsewhere in Canada

Saskatchewan was the first jurisdiction in North America to adopt a compulsory insurance scheme which included limited benefits paid to all victims without regard to fault. Not until 1970, did British Columbia and

1. Ontario Law Reform Commission, *Report on Motor Vehicle Accident Compensation*, Ministry of the Attorney General, 1973.

Manitoba introduce mandatory no-fault benefit coverage, followed by Ontario in January 1972 and Alberta in April 1972. Similar coverages are available on a voluntary basis in the Maritimes and until recently in the Province of Quebec. The plans in Saskatchewan, Manitoba and British Columbia are administered by provincial corporations.

Introduction of the no-fault element by the Provinces has been encouraged by recommendations of provincial commissions or committees set up to enquire into automobile insurance. A number of these committees have reached the conviction that the fault concept must be abolished completely in compensation for bodily injury, namely:

The Committee of Inquiry on Automobile Insurance, appointed by the Government of Quebec, Chairman J. L. Gauvin, report submitted March 1974.

The Sickness and Accident Insurance Committee, appointed by the Government of Saskatchewan, Chairman Judge A. Pope, report submitted September 1976.

The Advisory Committee on Reparations for Motor Vehicle Accidents, appointed by the Government of Saskatchewan, Chairman Roger Carter, Q.C., report submitted December 1976.

A Government White Paper on Accident and Sickness Compensation, Government of Manitoba, submitted May 1977.

Two of these studies have examined the wider question of compensation in all circumstances of accident and sickness. The Saskatchewan Sickness and Accident Insurance Committee, in particular, concluded that automobile injury compensation is an appropriate starting point in which to apply no-fault principles of reparation before extending the compensation scheme to all residents.

At this time, only the government of Quebec has committed itself to the substitution of a new basic no-fault plan for the current system based on the concept of responsibility. It has considered the problems of no compensation, partial compensation, and the delays of the fault system and decided to completely abolish the fault concept in compensation for bodily injury. Legislation to enact this change, and to transfer administration of bodily injury insurance to a public corporation, was passed by the Quebec National Assembly on December 22, 1977, and no-fault bodily injury coverage became effective on March 1, 1978. The Quebec initiative towards pure no-fault coverage for bodily injury is unique in North America.

3. U.S. Initiatives Towards No-Fault

In the United States, debate on the issue of no-fault culminated in the late 1960's, popularized by the Robert Keeton and Jeffrey O'Connell land-

mark study, *Basic Protection for the Traffic Victim*. This interest carried over to the Federal level, where the Department of Transportation was directed to conduct a two year study that resulted in the 1971 final report, *Motor Vehicle Crash Losses and Their Compensation in the United States*. The principal policy recommendation resulting from this study was:

That the existing system of insured tort liability should be supplanted by one based on first-party, no-fault insurance and that tort lawsuits and the adversary process should be eliminated for the mass of accidents.¹

Abolition of the liability insurance system and its replacement by a complete and integrated accident insurance plan not based on fault, was also proposed by the Insurance Commissioner of the State of New York in 1970 in a study titled *Automobile Insurance . . . for Whose Benefit?* This proposal was not enacted in its entirety but became an important document in the fault/no-fault debate.

Since 1970, when the Commonwealth of Massachusetts passed the first no-fault statute providing for a mandatory Personal Injury Protection Plan, 24 states have introduced no-fault elements into their automobile insurance requirements, while 16 states have so far legislated partial restriction on the recourse to tort action. No-fault bills have been introduced in every state but have failed to pass in some, in light of opposition from interest groups such as the trial bar, small and medium-sized insurance companies, and state and civil rights allies.

Table 3, showing no-fault features in Canada and in the United States is reproduced on the opposite page. The no-fault requirements in Michigan are the most far-reaching in effect in the United States today, and come closest to approximating the benefit levels and other elements set forth in the 1971 U.S. Department of Transportation study.

Interest in no-fault proposals in the United States is related partly to problems with the fault concept, such as difficulty in assigning fault, particularly under the rule of contributory negligence; court congestion, specifically in large urban centres; delay in paying claims; inefficiency and high cost of the fault system; inequity and distortion in payments; and duplication of benefits. Interest in no-fault is also complicated by other automobile insurance problems in the United States, such as the problem of the uninsured motorist; insolvent companies; and arbitrary cancellation of policies, all of which aggravate the inability of many injured victims to collect compensation. Therefore no-fault features have in many states been implemented as part of a package of limited compulsory insurance, to serve more as a palliative measure, providing some indemnity to every victim, rather than as a true effort to compensate without regard to fault.

1. U.S. Department of Transportation, *Motor Vehicle Crash Losses and Their Compensation in the United States*, report to Congress and the President by John A. Volpe, Secretary of Transportation, March 1971.

TABLE 3
AUTOMOBILE INSURANCE PLANS WITH NO-FAULT
ACCIDENT BENEFIT PROVISIONS
CANADA AND THE UNITED STATES**

	BASIC NO-FAULT BENEFITS			RESIDUAL RECOVERY FROM THIRD-PARTY				Effective Date Compulsory No-Fault
				Minimum Liability Coverage for injury	Threshold for Recovery of Non-Economic Loss		Severe injury or Death	
	Medical Costs	Wage Loss Limit	Survivors Benefits (1)		Medical Costs	Length of Disability		
<u>Canadian Jurisdictions</u>								
Ontario (Jan. 1978)	\$5,000	\$70/wk./104 weeks	\$5,000 + \$1,000	\$100,000 (v)	-----No Limitation-----			1972 (c)
Quebec (Prior to Mar./78)	choice	\$35/wk./104 weeks	\$5,000 + \$1,000	\$35,000 (v)	-----No Limitation-----			1970 (v)
Maritimes (3)	\$2,000	\$35/wk./104 weeks	\$5,000 + \$1,000	(2) (c)	-----No Limitation-----			1969 (v)
Manitoba	\$2,000	\$75/wk./lifetime	\$5,000 + \$1,000	\$50,000 (c)	-----No Limitation-----			1970
Saskatchewan	\$4,000	\$60/wk./lifetime	\$7,500 + \$1,500	\$35,000 (c)	-----No Limitation-----			1946
Alberta	Unlimited	\$50/wk./104 weeks	\$5,000, \$100/104 wks. + \$1,000	\$50,000 (c)	-----No Limitation-----			1972
British Columbia	\$50,000	\$75/wk./104 weeks	\$5,000, \$75/104 wks. +\$1,000, \$15/104 wks.	\$75,000 (c)	-----No Limitation-----			1970
<u>U.S. Jurisdictions</u>								
Colorado	>\$0,000	\$125/wk./52 weeks	\$1,000	\$15/30,000	\$500	52 weeks	X	Apr./74
Connecticut	*	\$5,000	*	\$20/40,000	\$400		X	Jan./73
Florida	*	\$5,000	None	\$10/20,000			X	Oct./76
Georgia	\$2,500	\$200/wk., \$5,000 max.	\$1,500	\$10/20,000	\$500	10 days	X	Mar./75
Hawaii	*	\$200/wk., \$15,000 max.	*	\$25,000	\$1,500		X	Sept./74
Kansas	\$4,000	\$163/wk./52 weeks	at wage loss limit	\$15/30,000	\$500		X	Feb./74
Kentucky	*	\$200/wk., \$10,000 max.	at wage loss limit	\$10/20,000	\$1,000		X	July/75
Massachusetts	*	\$2,000	*	\$5/10,000	\$500		X	Jan./71
Michigan	unlimited	\$363/wk./3 years	at wage loss limit	\$20/40,000			X	Oct./73
Minnesota	\$20,000	\$200/wk., \$10,000 max.	\$400/wk., \$10,000 max.	\$25/30,000	\$2,000	60 days	X	Jan./75
Nevada	*	\$175/wk., \$10,000 max.	\$5,000	\$15/30,000	\$750	180 days	X	Feb./74
New Jersey	unlimited	\$100/wk./52 weeks	at wage loss limit	\$15/30,000	\$200		X	Jan./73
New York	*	\$250/wk./3 years, \$50,000 max.		\$10/20,000	\$500		X	Feb./74
North Dakota	*	\$150/wk./\$15,000 max.	*	\$10/20,000	\$1,000	60 days	X	Jan./76
Pennsylvania	unlimited	up to \$15,000	up to \$5,000	\$15/30,000	\$750	60 days	X	July/75
Utah	\$2,000	\$150/wk./52 weeks	\$2,000	\$15/30,000	\$500		X	Jan./74
Proposed National Standard (Senate Bill 1381, House Bill 6601)	\$100,000 or 2 years' expenses up to \$250,000	\$250/wk./1 year adjusted by state incomes		\$15/30,000		180 days	X	Proposal

* Included in maximum under wage loss

** States with Restriction on Tort Rights

(1) Principal benefit + dependant benefit

(2) P.E.I. and N.S. \$35,000; N.B. \$50,000; Nfld. \$75,000

(v) Voluntary

(c) Compulsory

(3) New Brunswick is increasing No-fault
Benefits to: \$20,000 for medical costs
within 3 years; \$105/wk./156 wks. for
loss limits.

The release in June 1977 of a second Department of Transportation study which examined the experience of the 16 no-fault states over the 1971-1977 period, has renewed the no-fault debate in the U.S. This study, summarizing existing material on state plans, concluded that "no-fault works".¹ In addition, the Carter administration in the summer of 1977 indicated that it is in favour of passing a bill that will set minimum federal standards for state no-fault insurance for personal injury. A version of this bill, known as the "National No-Fault Motor Vehicle Insurance Act" was passed by the United States Senate in 1974 but did not receive subsequent approval by the House of Representatives.

Similar legislation is currently before the Senate (S. 1381) and another virtually identical bill is before the U.S. Congress (H.R. 6601). This legis-

1. U.S. Department of Transportation, *State No-Fault Automobile Insurance Experience, 1971-1977*, June 1977.

lation requires all automobile insurers to provide no-fault accident benefit coverage on a compulsory basis and it requires the individual states to introduce restrictions on the right to sue for damages arising out of injuries sustained in automobile accidents.

The question of mandatory legislation relative to no-fault does not appear to be a primary problem. The principal debate appears to focus upon whether states should introduce such legislation individually or whether the Federal Government should introduce overall legislation with which all states would be expected to comply.

4. No-Fault in New Zealand, Australia and Great Britain

Until recently, the major step in pure no-fault enactment had taken place in New Zealand. The New Zealand system of compensation is of special interest as it protects residents not only from losses suffered as a result of motor vehicle accidents, but provides compensation without regard to fault for persons injured in every incidence of an accident. Since April 1, 1974, this integrated income protection and personal rehabilitation plan has been operating in New Zealand under the Accident Compensation Act. It has three objectives: 1) to provide prompt, fair and reasonable compensation; 2) to promote prompt and effective rehabilitation; and 3) to promote safety in every walk of life.

Fundamental to the operation of this system is the abolition of the common law action for damages, and the establishment of a more realistic and generous system of benefits. The application of the New Zealand system to motor vehicle injuries is demonstrated in this section and in Appendix A in comparison to other proposals for reform of auto accident reparation.

It is significant to note that damage to property is not covered by the New Zealand Act. Third-party liability property damage insurance and collision coverage apply in the conventional manner without any "no-fault" provision. Coverage can be obtained from the State Insurance Office or from private industry insurers.

A similar approach to compensation has been proposed in Australia in the 1974 study, *Compensation and Rehabilitation in Australia—Report of the National Committee of Inquiry*. The main thrust of this report was for creation of a compensation scheme to cover disabilities arising from illness as well as from injury. Dissolution of Parliament and a change of Government interrupted passage of legislation in 1974. Internal work on development of an improved compensation system appears still to be underway although plans for implementation appear to be postponed indefinitely, due in part to economic constraints.

Prior to the Australian Report, the Council of Justice in the United Kingdom submitted in July 1973 to the Royal Commission on Civil Liability

and Compensation for Personal Injuries, a report titled *No-Fault on the Roads*. This report recommended that a no-fault scheme should replace the present action in tort in Great Britain. Among its specific recommendations was the establishment of a tribunal or board to evaluate intangible losses that would be paid on a first-party basis. In addition, it recommended *full* payment of losses on an earnings-related basis to all injured persons. However, this report as a whole did not form the opinion of the Royal Commission.

In March 1978, the Royal Commission released its own report on *Civil Liability and Compensation for Personal Injury* and recommended that the "no-fault" compensation scheme for motor vehicle injuries should be modelled on the scheme proposed for work injuries, with benefits at broadly the same level. Special provision, however, would be made for children and non-earners including housewives and retired persons. The scheme would be administered by a government agency and would be financed by a gasoline tax.

The Royal Commission recommended that tort rights should be retained but that the function of the tort system should be one of supplementing the no-fault system of social security. All social security benefits should be offset in full against tort awards. Furthermore, the Royal Commission recommended that there should be a three month 'time threshold' for damages for non-pecuniary loss, thereby eliminating minor claims for pain and suffering.

5. Features of Selected Automobile Insurance Plans and Proposals

Substantial detail is provided in the charts which accompany this section as a reference to illustrate the numerous options available for reform of the automobile accident compensation system. The plans and proposals presented in Table 19 and in Appendix A correspond to selected developments in no-fault proposals and to submissions received by the Select Committee in its recent hearings on the no-fault issue. They are divided into three groups:

1. *Recommendations for Enrichment of First-Party Benefits in Ontario*
 - Current Ontario insurance coverage and benefits.
 - Select Committee recommendations, 1977, for enriching Accident Benefits (with reference to new benefit payments to be effective July 1, 1978).
 - The Advocates Society of Ontario proposal for enriching Accident Benefits levels, based on 1974 recommendations.
2. *Proposed or Existing Plans Suggesting a Mixed Fault/No-Fault Approach to Compensation*
 - The J.B.M. Murray proposal.
 - Variplan: Insurance Bureau of Canada proposal.

TABLE 19
COMPENSATION FOR BODILY INJURY
METHODS OF RECOVERY UNDER SELECTED
AUTOMOBILE INSURANCE POLICIES AND PROPOSALS

TERMINI OF PROPOSED PLAN	RECOVERY FROM OWN INSURER			RECOVERY FROM PARTY AT FAULT			THRESHOLD TO TORT
	Basic Benefits Economic Loss	Extended Economic Benefits	Benefits for Non- Economic Loss	Threshold To Tort	Excess Economic Loss and Non- Economic Loss		
	Medical Limit	Wage-loss Limit per week (Year)	Remained Options	Maximum Provided	Description Opposite	Minimum Disability Insurance Limit	
ONTARIO (CURRENT)	\$ 5,000	5.70-2 years				\$100,000	(1) Varipian
SELECT COMMITTEE PROPOSAL	\$25,000 *	\$140-2 years *				Unlimited	Death, serious permanent injury, which includes substantial disfigurement, and prolonged disability continuous for more than 120 days.
ADVOCATES SOCIETY PROPOSAL	\$ 5,000	\$119-no limit				\$100,000	(2) Michigan
J.B.M. MURRAY PROPOSAL	\$100,000 combined		Medical and Wage-loss			Unlimited	(3) Proposed U.S. National Standard
VARIPIAN - I.B.C. PROPOSAL	\$20,000	\$200-3 years			1	\$100,000+	For economic loss: no threshold. For non-economic loss: serious and permanent injury resulting in substantial and medically demon- strable permanent impairment affecting resumption of customary activities; permanent loss of important bodily function.
MICHIGAN (CURRENT)	Unlimited	\$34-3 years			2	\$ 20,000	Significant permanent wasting or disfigurement; death or disability continuous for more than 180 days.
PROPOSED U.S. STANDARD	\$100,000 or 2 Yrs.	\$250-1 year	Medical and Wage-loss		3	\$ 15,000	
NEW ZEALAND (CURRENT)	Unlimited	\$24-no limit	Wage Loss	\$17,000			
SASKATCHEWAN PROPOSAL	Unlimited	\$185-5 years	Wage Loss	\$15,000			
QUEBEC (NEW LEGISLATION)	Unlimited	\$100-5 years	Wage Loss	\$20,000			
ONTARIO LAW REFORM COMMISSION	Unlimited	\$250-no limit	Wage Loss				

* Effective July 1, 1978

- Current compulsory insurance coverage in the state of Michigan.
- Proposed U.S. National Standard for automobile insurance.

3. Plans or Proposals Approximating A Pure No-Fault Method of Compensation

- Current accident compensation plan in New Zealand, as applied to automobile accident injuries.
- Saskatchewan Automobile Reparations proposal, 1976.
- Legislation for the reform of compensation for bodily injury in the Province of Quebec, passed December 1977.
- Proposal of the Ontario Law Reform Commission, 1973.

The thrust of the no-fault initiative in automobile insurance has been for reform of the system of compensation for bodily injury. The reliance on first-party benefits and/or on third-party recovery in the eleven plans selected for review in this section is illustrated in Table 19.

A low level of first-party benefits is currently available in Ontario, compared to plans or proposals in the other jurisdictions shown. This low level of benefits which will be increased on July 1, 1978 supplements access to recovery of loss from the party at fault. Schemes which limit or eliminate recovery from the party at fault, as in Michigan or Quebec, necessarily provide a higher level of first-party indemnity.

Further details of first-party benefits are presented in Tables 1 to 7 of Appendix A, under the headings of:

1. Medical, Hospital and Rehabilitation Expense
2. Wage Loss Benefits for the Totally Disabled Wage-Earner
3. Wage Loss Benefits for the Partially Disabled or the Non Wage-Earner
4. Compensation for the Death of a Family Member, and
5. Benefits for Non-Economic Loss

Specific comments under the five categories of loss, as reviewed in Appendix A, are presented here.

Medical, Hospital and Rehabilitation Expense

— Table 1 of Appendix A shows that no-fault proposals generally provide unlimited medical coverage with no time limit. Costs of unlimited coverage are said to be contributing significantly to increased insurance costs in the three states of Michigan, Pennsylvania and New Jersey which have unlimited coverage provisions.

It is important to note that the Michigan Insurance Department has cited a 1975 NAIH study to the effect that the total cost of medical claims exceeding \$25,000 in Michigan is \$8 per car per year.¹ Recent statements from the Detroit Automobile Insurance Exchange have been quoted before the Select Committee, indicating that the cost has risen to around \$20 per car per year.² This amount is high relative to the total Accident Benefits loss cost in Ontario of about \$10 per car insured, but may not be out of line if consideration is given to the lack of a public health insurance scheme in the United States.

In the U.S. unlimited medical coverage is making it difficult for insurers to set aside contingent reserves with sufficient confidence about the limit to their exposure. In addition, small companies with a number of "catastrophic" injury claims encounter problems of reinsurance. As indicated in Section F, these problems may not be equally applicable in Ontario.

— Sickness and accident plans providing medical coverage are allowed to subrogate the auto insurer in Ontario today. Pure no-fault proposals, as in New Zealand and in Quebec, provide medical benefits in excess of government health insurance benefits and eliminate subrogation.

1. Insurance Bureau, Michigan Department of Commerce, *No-Fault Insurance After Three Years: A Report to the Governor*, October 1976, in Department of Transportation, *op. cit.*, 1977.
2. Proceedings of the Select Committee on Company Law, Ontario Legislature, August 31, 1977, CL-1035-1.

The J.B.M. Murray proposal suggests that other insurance coverages be primary, and that the vehicle owner be allowed to choose a larger deductible if he is covered under other health or wage continuation plans. It is unclear whether this deductible would apply to injuries sustained by pedestrians or occupants of the vehicle. This suggestion introduces problems of coordinating coverage but experience in Michigan has demonstrated that coordination can provide savings to the consumer.

Wage Loss Benefits for the Totally Disabled Wage-earner

- Table 3 of Appendix A points out that the current Ontario weekly wage loss limit is significantly below that of no-fault proposals and mixed fault/no-fault plans. This limit does not deny the innocent victim full indemnity as he has the right to tort recovery, but it is greatly inadequate for the average Ontario resident with more than minor injuries, who earned an average industrial wage of \$252 in 1977, and who cannot put the blame for his accident on another driver.
- Three of the pure no-fault approaches to compensation also set a *minimum* limit on weekly indemnity to safeguard the low income earner.
- The Variplan proposal and certain no-fault schemes provide for a 7-day waiting period before payment is made. The Insurance Bureau of Canada, sponsor of Variplan, indicates that the waiting period is a means of avoiding small insurance claims with high administrative expense relative to the small wage loss settlement. The waiting period is in effect a "disappearing deductible", as the first week's wage loss is regained if disability continues past 7 days.
- As benefits are non-taxable in Ontario and in many other jurisdictions, most plans reduce the gross salary eligible for reimbursement by 10% to 20% to derive a net benefit payable. The Quebec proposal further reduces the benefit payable to 90% of net income to discourage continuing reliance on insurance payments.
- Ontario sets a two year time limit for no-fault disability payments. Permanent disability qualifies for continued benefits under social assistance programmes if compensation has not been obtained from the party at fault. Variplan and the plan in Michigan extend first-party benefits for an extra year. Two of the pure no-fault plans and the recommendations of the Advocates Society suggest unlimited periods of eligibility in the case of permanent incapacity. While Saskatchewan and Quebec place five year limits on wage loss payments, these limits actually serve as a date for review of the status of the injured person, after which time he can qualify for long-term disability payments.

Wage Loss Benefits for the Partially Disabled or the Non Wage-Earner

- The method most often used for indemnifying the partially disabled provides that any income earned reduces the gross earnings available for

compensation. The Quebec proposal departs from this method by specifying a formula for reducing disability payments from the level payable in case of total incapacity. (Refer to Table 4 of Appendix A.)

- Benefits, when payable to the unemployed, are frequently based on income earned in previous employment. It should be noted that Variplan does not propose to indemnify the unemployed, or other non wage-earners, except for replacement services actually hired.
- The pure no-fault plans provide some measure of compensation to non-earners with no current work experience. In particular, they attempt to provide reasonable indemnity to the young injured student as he/she may be deprived of the opportunity to earn income in the future by a permanent or severe injury. As the tort system assesses damages in these situations, a no-fault system may not be able to ignore this class of victim.

Payments under the no-fault schemes shown in Table 4 of Appendix A base payments on the age of the student or minor and some adjust these payments to reflect earning potential. The mixed fault/no-fault plans (Michigan and Variplan) exclude the student or minor from any recovery, unless the injury qualifies for tort recovery by meeting the threshold of serious injury.

- If a homemaker spouse is injured in an auto accident, wage-related losses are difficult to establish and are frequently disclaimed by the automobile insurance system. Instead, the family may be compensated for loss of services.

This same approach is adopted in many no-fault plans. Some plans provide for reimbursement only if actual replacement services are hired; while others provide as indemnity the cost of substitute services even if freely performed by other family members or friends.

The tort system may provide compensation to the homemaker if, for example, the court determines that loss of future income may occur because the homemaker is denied the opportunity to re-enter the labour force. This applies usually only in the case of prolonged disability. No-fault schemes in general have made no provision for this contingency. However, the compensation system in New Zealand does provide for a supplementary plan, which is separately subscribed to, that will indemnify the homemaker spouse in the event of continuing disability.

- Disability by non-employed persons over 65 is infrequently compensated. Benefits are normally available under government social assistance programmes or pensions.

In some no-fault plans, a measure of earner's benefits can be provided to extend compensation beyond age 65 if the accident occurs after that age. The Saskatchewan Reparations proposal, the current Quebec legislation, and the New Zealand plan suggest this solution. The O.L.R.C. proposal suggests wage-related indemnity after age 65 only if loss of opportunity for employment is established.

Compensation for the Death of a Family Member

- Compensation on death of a family member can be distributed as either a final fixed-sum payment or a continuing earnings-related benefit. As shown in Table 5 of Appendix A, partial no-fault systems normally provide first-party death benefits as an arbitrary lump sum to cover immediate expenses and as initial "consolation". Further recovery is expected to be pursued through tort action. In addition, mixed fault/no-fault plans generally specify death as a threshold for tort, also permitting further recovery from the party at fault.

Pure no-fault proposals substitute earnings-related compensation for lump sum death benefits. The New Zealand, Saskatchewan and O.L.R.C. plans also provide for an immediate 'nominal' amount to be paid upon death. Details are provided in Table 6 of Appendix A.

The pure no-fault approaches concentrate on indemnity in the case of death of a wage-earner contributing to family income. The death of non-contributors is compensated by arbitrary lump-sum payments or not at all (New Zealand).

Benefits for Non-Economic Loss

- Table 7 of Appendix A provides details of no-fault payments for non-economic loss in existing or proposed plans in New Zealand, Saskatchewan and Quebec. These three jurisdictions have decided that permanent loss or impairment of bodily function should be compensated to some extent on a first-party basis for the resulting pain, inconvenience, or loss of amenities.

The values established for non-economic loss are arbitrary and admittedly below potential tort recovery values. They are at best a minor solace but still are not an entirely meaningless contribution. They beg the question: is the claimant more content with or resigned to the disabling consequences of his injury if he receives \$100,000 for pain and suffering, than when he receives \$20,000?

Summary

In general, the tables in Appendix A point out the relative importance attributed to indemnity on a first-party basis, and the diversity in approach towards compensating different types of injured persons. Significant differences in the philosophy and objectives of compensation underlie the distribution of benefits between fixed-sum payments and earnings-related payments, between indemnity to wage-earners and compensation to non-earners, and between methods of reimbursement for non-economic loss.

In conclusion, this presentation of no-fault elements in eleven proposed or existing automobile insurance plans has shown a range of options for re-

forming bodily injury compensation in the automobile insurance system. Many of these choices are based on value judgements.

I. NO-FAULT INSURANCE FOR PROPERTY DAMAGE

1. Introduction

In a uniform system of no-fault, compensation for property damage would be based upon the same principles as payment for losses from injury. That is, under a uniform pure no-fault approach to automobile insurance, the right to recover from third parties through the law of liability is completely taken away for property damage as well as for bodily injury claims. All third-party negotiations or lawsuits for recovery of loss are replaced by first-party settlements between the person suffering loss and the insurer of the vehicle involved in an accident.

But the nature of the damage and the repercussions of property damage accidents on the individual and on society differ from those associated with bodily injury. Accordingly, no-fault insurance for property damage cannot be justified on the primary principle that all victims should be entitled to compensation for their loss.

Instead the emphasis of no-fault is directed to reducing the extensive and escalating losses that result every year from damage to vehicles. In Ontario, 60% of all compensation paid by insurers under the present system is accounted for by property damage losses. Similarly the major part of the automobile insurance premium is paid to cover damage to property. If savings in property damage losses and premiums can be achieved, then it is possible that these savings can be applied to improve injury benefits without undue financial burden on the motorist.

The importance of savings in property damage is further explained by the fact that motorists use the automobile insurance product most frequently for vehicle damage claims. Property damage claims outnumber bodily injury claims in Ontario by a ratio of eight to one. The motorist who pays automobile insurance premiums year after year often feels that he is not getting his money's worth if he experiences delays, inconvenience, or denial of his claim. Accordingly, the need for improvement in the speed and efficiency of the claims settlement process is another key factor in the consideration of no-fault principles with respect to property damage.

Given the importance of savings in property damage both to the automobile insurance system and to the individual driver, the consideration of no-fault should not be restricted to the area of bodily injury only. As will be shown later, several jurisdictions with no-fault elements in their automobile insurance systems have decided to retain the fault concept for property damage, for the practical reason that no-fault property damage insurance is frequently misunderstood by the motoring public. This does not necessarily indicate that no-fault applied to property damage fails to meet its objectives.

2. The Savings Objectives of No-Fault for Property Damage

Aside from the principle of uniformity stating that fault should be completely taken out of compensation for motor vehicle accidents, savings are the primary objective in consideration of a no-fault plan for property damage. There are several ways in which a no-fault approach can produce savings, as outlined below.

Simplifying the Claims Adjustment Process

With no-fault coverage, the vehicle owner needs only to have the damage to his vehicle appraised in order to submit a claim to his insurer. He no longer is required to go through a claims adjustment process. For example, if a driver takes his car to an appraisal centre, he can at the same time fill in his claim and direct it to his insurer without the necessity for *any* further investigation of the accident. As a result, much claims processing time and investigative expense is saved.

It should be noted that a similar settlement process is operated by the government-managed insurance systems in Manitoba, Saskatchewan and British Columbia. These systems permit a one stop settlement process from the claimant's point of view, and they simplify, although they do not eliminate, the adjusting function.

With no-fault coverage, insurance company adjusters no longer need to spend time in negotiations regarding which insurer is responsible for payment of claims. Despite the fact that close to three-quarters of Ontario vehicle owners already purchase first-party collision coverage, subrogation between insurers on collision claims and its associated costs are not eliminated under the present system. In an effort to reduce inter-company disputes over fault and to keep costs of settlement low, Ontario insurers are making increased use of the "inter-company settlement chart" or "collision assessment chart". Nevertheless, certain claims continue to result in dispute and fault investigation.

Legal Fees and Court Costs

Under no-fault insurance, companies and vehicle owners avoid legal expense in settling vehicle damage claims. However, it is estimated that less than 10% of the 143,000 third-party property damage claims processed in Ontario in 1976 involved legal advice. Therefore, the saving in this category may be minimal.

Despite low legal involvement, the public still benefits by a reduced load on the court system as many claimants use the small claims and other lower courts for recovery of their deductible, or to disprove liability in order to escape higher premiums. Under no-fault plans that permit deductible recovery, the vehicle owner recovers directly from his own insurer and is not obligated to deal with a third-party insurer, or forced to go to small claims court.

Rating Methods and Control Over Repair Costs

No-fault property damage insurance encourages the introduction by insurers of a rating system which is specific to the repair costs and safety features of each vehicle insured. In Michigan, for example, "first-party collision insurance is priced in relation to the value of the vehicle. Owners of higher priced vehicles in Michigan pay relatively larger premiums than owners of older, lower-valued vehicles. Thus, more equity is introduced into the system".¹ By recognizing the importance of safety factors in setting premium rates, the no-fault plan intends to discourage the consumer from driving a vehicle which is costly to insure and which contributes most to total vehicle damage losses.

It can be argued that a similar incentive to reduce collision costs already exists under first-party collision coverage. However, under collision coverage, the insurer often pays his policyholder's claim with funds that he then recovers from the insurer of the party at fault. That is, he is paying his policyholder with another person's money and consequently may not be concerned about controlling the appraisal process and the costs of repair. As a result, the incentive to contain costs under collision coverage is not as apparent as under no-fault coverage, where the insurer is, in all cases, accountable to his own policyholder for rising costs.

Insufficient Evidence Regarding the Savings of No-Fault

Despite the above advantages, a no-fault property damage plan will not create the major savings in claims adjustment costs and legal expenses that occur under no-fault compensation for bodily injury. The potential for major gains in efficiency is less because proportionately fewer claims involve legal advice, and techniques within the fault system, such as the collision assessment chart, can be more readily applied to reduce claims adjusting expenses.

Experience in the jurisdictions of Florida, Michigan and Massachusetts, which have at some time implemented forms of no-fault property damage insurance, unfortunately has not produced sufficient analyses of the efficiencies created by a transfer to a single system of compensation for vehicle damage losses. A study of no-fault experience in Florida, which did look at property damage separately, found that coverage for property damage expanded under Florida's optional no-fault law but was not accompanied by any important reductions in processing costs.² These findings are affected, to some extent, by the high frequency of claims experienced in Florida, and by the structure of the "no-fault" plan for property damage which was made up of a number of options combined with varying degrees of deductible re-

1. Jones, Thomas C., Commissioner of Insurance, State of Michigan, *No-Fault Automobile Insurance in Michigan: A Preliminary Study*, 1976.
2. Little, Joseph W., "No-Fault Auto Reparation in Florida: An Empirical Examination of Some of Its Effects", reprinted in Council on Law-Related Studies, *No-Fault Automobile Insurance in Action*, *op. cit.*

covery based on fault. As a result, the Florida study was not able to demonstrate clearly whether or not no-fault property damage insurance brings about the efficiency theoretically attributed to it.

Massachusetts is another important example of a state that has experimented with no-fault. Massachusetts originally placed vehicle damage insurance under its no-fault law but later in January 1977 returned property damage coverage to the fault system. The Select Committee in its recent meetings in that state heard some of the reasons behind the original intent of no-fault for vehicle damage and the subsequent experience that led to a switch back to the fault system. A 1977 U.S. Congressional Sub-Committee report on Massachusetts no-fault property damage experience concluded that:

"In sum, the Massachusetts experience with property damage no-fault was too short to come to any firm conclusions, although it does appear that the system worked to keep down rates when it was being run properly."¹

The measurement typically examined to determine the savings resulting from the elimination of fault in property damage settlements is a decrease in premium rates. Any analysis of overall premium and rate levels in recent years has been unfortunately distorted by inflationary factors, obscuring the changes in real costs. In Michigan, for example, where no-fault collision and comprehensive coverage is provided on an optional basis compared to mandatory requirements for no-fault bodily injury coverage, rampant inflation in automobile repair costs has been quickly passed on to the consumer in higher premiums, whereas insurers have maintained relatively stable rates for mandatory injury coverage, despite similar levels of inflation in medical care costs and wage indemnity.² The effect was one in which total premiums increased but injury no-fault coverage was subsidized by vehicle no-fault coverage, confusing any analysis of cost savings.

Accordingly it should be emphasized that overall premium rates under no-fault are not necessarily expected to decrease if rates are to fairly reflect levels of inflation. Rather, the ratio of benefits paid to premiums earned is expected to increase (without underwriting loss to the industry).

To recapitulate, the potential for reducing the cost of claims for property damage under no-fault is not as high as in the area of compensation for bodily injury. The principal opportunity for savings remains in the area of inter-company subrogation. Under the collision coverage currently offered in Ontario, each insurer normally pays his own policyholders directly for all their losses (excluding the deductible), but is permitted to subrogate the insurer of the party at fault for reimbursement. A no-fault proposal for vehicle damage insurance eliminates the right to subrogation for collision claims;

1. U.S. Congress, *Congressional Record—Extensions of Remarks*, E4032, June 23, 1977.

2. Jones, Thomas C., Commissioner of Insurance, State of Michigan, *op cit*.

that is, the insurer cannot seek any reimbursement for his policyholder's claim from the party at fault. As a result, considerable expense in closing claim files can be eliminated, increasing the ratio of benefits paid per premium dollar.

A further thrust of no-fault for property damage is to establish a uniform method of compensation for all types of losses that completely eliminates the right to sue, and to promote a more efficient and equitable method of rating that matches premiums charged to the specific vehicle for which damages are paid.

3. Cost Redistribution and Choice of Coverage

A major impact of no-fault insurance for vehicle damage is on the redistribution of the premium burden. The following two concerns were discussed in Section E under bodily injury, but are reiterated here with specific reference to property damage.

One concern is the matter of the driver's *accident or claim record* as a rating criterion. Under the fault system, drivers with at-fault claim records are assessed a higher premium than drivers with claim-free records. Under a no-fault system, use of claim records as a rating criterion would penalize the driver who submits claims for accidents which are not the result of his fault. Accordingly, the claim record is disregarded in assessing premiums, such that the higher premiums presently paid into the insurance pool by careless drivers may have to be replaced under the no-fault system by higher average premiums for the claim-free driver.

A second concern is related to the fact that *non-private passenger vehicles* cause a significant amount of the damage to private passenger vehicles. Under a no-fault system, the funds that insurers of commercial vehicles contribute towards the damages incurred by private passenger vehicles will not be available since subrogation rights are eliminated. Unless rates for commercial vehicles are increased to reflect the greater potential for damage to other property, private passenger vehicles may be subsidizing commercial vehicles under the no-fault system. The converse situation is evident in the case of light vehicles, such as motorcycles.

Thirdly, redistribution of the premium burden becomes an even more important issue when the question is raised whether no-fault insurance for vehicle damage should be made compulsory or optional.

Compulsory Coverage

If vehicle damage coverage under no-fault is made compulsory, a large number of new insureds are introduced who must bear a premium burden substantially higher than under the prior fault system. At present about one-quarter of Ontario vehicle owners choose not to purchase first-party collision coverage. They rely instead on recovery under the third-party liability

insurance of the party at fault. Many people who currently do not carry collision coverage are uninsured because they cannot afford to buy such insurance, either because of low income or because they are categorized as high risk drivers. Others do not insure their vehicle because the cost of such insurance is too high relative to the value of an aging or defective car. These uninsured drivers have a chance for recovery under the fault/liability system, but under the no-fault system they lose this chance.

TABLE 20
APPARENT DISTRIBUTION OF LOSS COSTS FOR PROPERTY DAMAGE

	1975 Losses Incurred in Ontario (\$ million)		Distribution of Losses Under Compulsory No-Fault Insurance (\$ million) Recovery From Collision Insurer	
	At Fault— Recovery from Collision Insurer (1)	Not at Fault— Recovery from Liability Insurer** (2)	No Deductible Recovery (1) + (2)	Deductible Recovery (1) + (2)
<i>Driver Presently with Collision Coverage</i>				
Damage	\$177	\$ 70	\$187	\$187
Deductible	—	21	—	21
<i>Driver Presently without Collision Coverage</i>				
Damage	38*	23	61	61
Deductible	—	7	—	7
<i>Total Losses Incurred</i>	<u>\$117</u>	<u>\$121</u>	<u>\$248</u>	<u>\$276</u>
Cars insured (millions)	2.075	2.750	2.750	2.750
Loss costs per insured car	\$56.00	\$44.00	\$90.00	\$100.00

* No Recovery, driver assumes own loss.

** Includes an amount for property damage other than vehicle.

Source: Insurance Bureau of Canada.
For estimates see Appendix C.

Table 20 illustrates the effect of compulsory vehicle damage coverage on the Ontario driver. Based on 1975 industry data, the Ontario driver who purchases only liability coverage to protect himself in the event that he causes damage to another vehicle, pays a "proxy" premium rate of \$44.00 in loss costs per insured vehicle. In contrast, 75% or so of vehicle owners, who currently purchase both collision and liability coverage, pay premiums to support roughly \$100.00 in loss costs per insured vehicle. Table 20 shows, in simplified fashion, that the one-quarter of owners who now pay premiums to cover \$44.00 in liability loss costs will be required to pay \$100.00 under compulsory no-fault coverage for full collision protection.

This major increase in premium burden is mitigated somewhat if deductible recovery is denied.

Optional Coverage

On the other hand, if no-fault vehicle damage insurance is made optional, a vehicle owner who is not insured against damage to his own car cannot sue anyone else for recovery and must bear his own loss. He can therefore be faced with the widely disparate choice of no coverage and no recovery, or coverage at a higher premium level. Witnesses before the Select Committee have testified that removal of the right to recover for damage to motor vehicles has brought angry reaction, in both Michigan and Massachusetts, from motorists who do not have collision coverage and cannot collect from the negligent driver.

The solution most appropriate to encouraging the driver to elect to buy no-fault coverage is to make it affordable. The common method of improving affordability in either compulsory or optional plans is to subsidize the high-risk driver so he can afford to protect his own car. This solution offers no relief to the low income earner who continues to be told: "if you can afford a car, you can afford insurance". In any case, redistribution of the premium burden resulting in subsidization of high-risk drivers is considered in many jurisdictions to be unacceptable to a significant proportion of the motoring public.

To resolve these problems and complaints, many proposals for no-fault have favoured a partial no-fault approach that provides an intermediate level of coverage which pays for losses only in predefined, blameless or shared blame accident situations. This intermediate level of coverage is priced to correspond roughly to the current cost per insured vehicle of liability coverage. The intermediate or limited collision coverage acts as a substitute for liability coverage, allowing the vehicle owner to recover from his own insurer (rather than from the insurer of the party at fault, as under liability coverage) when an accident is not his fault. Deductible recovery may or may not be included.

Numerous variations of the limited collision option under no-fault can be drawn up to incorporate a variety of "blameless" loss situations. The Variplan proposal illustrated in Table 8 of Appendix A is one example of a plan that provides a staged approach to no-fault property damage insurance. Table 21 presents a comparison of premium costs between 1974 property damage coverages available in Ontario and those available under Variplan. Partial coverage under Plan C permits a vehicle owner to spend no more on property damage premiums under the no-fault system than he would under the fault system and still obtain some recovery for damage to his car.

TABLE 21
COMPARISON OF COSTS PER INSURED VEHICLE FOR VARIPLAN AND THE PRESENT ONTARIO
PLAN, AS OF 1974

	73% With Collision Coverage	27% Without Collision Coverage
<i>Present Plan</i>		
Liability Coverage for Property Damage	\$ 51.35	\$51.35
Collision Coverage	67.10	—
	<u>\$118.45</u>	<u>\$51.35</u>
<i>Variplan</i>		
Partial Collision Coverage (Plan C)	—	\$47.78
Full Collision Coverage (Plan A)	\$118.30	—
Residual Property Damage (Other than moving vehicles)	2.46	2.46
	<u>\$120.76</u>	<u>\$50.24</u>

Source: Exhibit 13-B, Proceedings of the Select Committee on Company Law, August 23, 1977.

Should There Be A Choice of Coverage?

The question of choice of coverage for damage to vehicles can also be addressed separately from its immediate cost implications. The reasoning behind compulsory no-fault insurance is to ensure that no blameless driver under the more efficient no-fault system is left without a recourse to some method of recovering his loss. Optional coverage can leave the driver with the widely disparate choices of full recovery or no recovery.

The Quebec Inquiry on Automobile Insurance has pointed out that despite the importance of property damage in terms of total costs, the losses arising from damage to an automobile rarely have drastic consequences for an individual. Therefore there appears to be no justification for requiring that an individual be forced to protect his investment in the value of his automobile. The Quebec report concludes that the automobile plan "must give the owner of an automobile the possibility of limiting the circumstances under which he chooses to be protected by insurance against property damage to his vehicle".¹

This recommendation is not in conflict with the concept of no-fault insurance. Rather it implies that the no-fault system must provide the type of coverage demanded by the consumer, at a premium burden which the consumer will find acceptable. It ties back into the earlier discussion on premium costs and suggests that no-fault insurance for property damage should present a number of options: full coverage, limited coverage or even no coverage, to correspond to the recovery expectations and "pocket-book" of the motorist.

1. Government of Quebec, *Report of the Committee of Inquiry on Automobile Insurance*, March 1974, page 306.

4. Deductible Recovery

Under strict no-fault proposals there can be no deductible recovery. The person ostensibly to blame for an accident is no longer obligated by law to pay either the full loss or the deductible portion to the blameless driver.

As a result, the size of the deductible becomes an important matter to be considered in any no-fault proposal. The standard level of the deductible is generally dictated by the need to minimize the average cost of vehicle damage insurance. A high deductible would be justified by the desire to keep minor claims out of total claims payout, thereby reducing claims' processing costs and total losses paid for by the policyholder. Under the fault system, the motivation for a high deductible is even greater, as fault investigation in minor claims contributes heavily to the overall expenses of the liability system. The Select Committee in its First Report on Automobile Insurance recognized this problem and recommended (although with dissenting opinion) that the minimum allowable deductible be raised to \$250, in order to ease premium costs for the motoring public.¹

However, if "buy-down" of the deductible is not permitted and the strict no-fault requirement of no deductible recovery is maintained, then the no-fault proposal may encounter a frequently voiced criticism: the insured driver is likely to complain that he is not getting his money's worth for insurance coverage, if he is denied recovery of the deductible amount when the accident is not his fault.

In effect, the owner is probably saving money on his premium cost, because elimination of deductible recovery reduces the total losses paid out for damage to vehicles. This is illustrated in Table 20 where the loss costs per insured vehicle are \$90.00 without deductible recovery, increasing to \$100.00 with recovery.

To reduce complaints, the concept of the "fault deductible" has been introduced. A "fault deductible" does not necessarily contradict the no-fault approach to vehicle damage. The pure no-fault principle, which requires complete restriction of tort and payment by the vehicle owner's own insurer, can remain intact even though a fault deductible is applied.

With a fault deductible, an owner is ensured recovery of his deductible under standard rules, such as the rules on a collision assessment chart. In given circumstances, he can recover 100% of his deductible; in others, 50% or some other fraction. Payment is made by each insurer to its own policyholders. In a situation such as damage to a parked car, the owner of the parked vehicle could be guaranteed 100% recovery of his deductible.

1. The Select Committee on Company Law, *First Report on Automobile Insurance*, page 83.

The fault deductible does add extra processing time to first-party claims. In addition to an appraisal of damage, the vehicle owner must provide, in his claim, information on the circumstances of the accident. Insurance company adjusters must also devote time to verifying the events of the accident or obtaining police reports as a basis for apportioning fault, and may need to contact third parties for information.

TABLE 22
RECOVERY SITUATIONS UNDER NO-FAULT FOR PROPERTY DAMAGE
(No Right to Recover from Party at Fault)

Vehicle Owner's Coverage	Driver At Fault*	Driver Not At Fault*
A. Full Collision Coverage		
1. Amount in Excess of the Deductible	Yes	Yes
2. Deductible Amount: No Coverage	No	No
3. "Fault" Deductible Available	No	Yes
B. Limited Collision Coverage		
1. Amount in Excess of the Deductible	No	Yes
2. Deductible Amount: No Coverage	No	No
3. "Fault" Deductible Available	No	Yes
C. No Coverage		
1. Amount in Excess of the Deductible	No	No
2. Deductible Amount: No Coverage	No	No
3. "Fault" Deductible Available	No	Yes

* Based on Standard Recovery Rules.

No . . . the vehicle owner does not recover his loss.

Yes . . . the vehicle owner does recover his loss.

The concept of the fault deductible is generally applied only to vehicle owners who purchase some form of collision coverage. However, it can also be extended to all vehicle owners including those who do not elect to buy no-fault collision insurance. In such a case, it would probably apply only in readily defined blameless situations such as hit-and-run accidents and damage to parked cars.

If applied to all owners, the fault deductible can be made mandatory, together with or as part of the compulsory no-fault policy for bodily injury. A small incremental premium would be charged. If such a fault deductible "policy" were made mandatory, every vehicle owner would be sure to recover up to the standard deductible amount (say, \$250 as recommended in the First Report), to the extent that an accident was not his fault.

Given a method of deductible recovery and given a choice of coverage, a no-fault plan for property damage can provide the same entitlement to recovery of losses (at about an equivalent cost) as a plan under the fault/liability system. Table 22 illustrates this observation by indicating the general types of no-fault coverage applicable to recovery in either a fault or no-fault situation.

5. Abuse of the No-Fault System

The success of a no-fault system for settling property damage claims can be imperiled largely by two factors: consumer dissatisfaction with coverage, and abuse or overutilization of the system. The preceding discussion demonstrated that no-fault coverage can be structured to meet the recovery expectations and pocket-book of the vehicle owner. The problem of abuse is more difficult to solve.

The problem of abuse arises because the no-fault system, by simplifying the claim adjustment process, makes it easier to take advantage of the system: no longer is it necessary to identify the circumstances of an accident to assist in the division of blame; no longer is there an irate third party trying to establish that the accident was not his fault. Under the no-fault system it is relatively easy to submit fraudulent or exaggerated claims (e.g. by declaring that damage was caused by a hit-and-run driver, or that a loss resulted from theft), as the insurance company is unlikely to investigate the incident. Massachusetts is an example of a jurisdiction that has experienced serious problems of this type. If own vehicle damage coverage is made compulsory, the potential for overutilization is increased, as some vehicle owners may attempt to "capitalize" on coverage they did not want to buy. British Columbia experienced this problem with compulsory comprehensive coverage under the fault system.

Abuse, if it occurs, will inflate total loss costs and increase the average cost of no-fault coverage for property damage. A number of possible solutions are suggested below. Each has its drawbacks, but it is important to note, at the same time, that the simple threat of penalty may be sufficient to deter all but a minimal portion of the vehicle owning public from overuse of the system. Possible means to control overuse include:

— Surcharges based on claims submitted.

This remedy has the inherent disadvantage that it penalizes the driver who submits a claim but is not to blame for the damage. A low surcharge on claims may be acceptable as just another form of deductible, but it is unlikely to have a "prohibitive" effect.

— No deductible recovery below the standard amount.

This remedy may be effective in discouraging some degree of abuse, but it is unlikely, for the same reason as the claims surcharge, to be acceptable to the blameless vehicle owner.

— A special fraud investigation unit and/or large fines assessed for fraud.

This remedy will only spot and penalize a small proportion of fraudulent or exaggerated claims, unless a significant budget is allocated to the investigative unit.

— Requirement that all accident situations including unwitnessed accidents and all thefts be reported to the police.

This remedy is likely to deter a significant portion of abuse but may require greater police involvement in very minor damage situations.

It is difficult to predict what extent of abuse, if any, might develop in the Province of Ontario under a no-fault property damage system. It may be that the threat of large fines and the existence of a limited measure of fraud investigation might be sufficient to make the problem of overutilization of little consequence in this Province.

6. Coverage for Vehicle Damage in Other Jurisdictions

Table 8 of Appendix A illustrates the features of eleven selected plans that provide protection to the vehicle owner against damage to his own car. Five of the plans shown eliminate the right to sue for damage to vehicles. Two of the five provide for compulsory coverage. Under the plans in the remaining three jurisdictions, a driver not electing to purchase coverage chances no recovery, even in a situation in which he is not to blame.

It is interesting to note that damage to the vehicle or other property is not covered by no-fault legislation in either New Zealand or Quebec. Third-party liability insurance is made compulsory and is limited to property damage only. Collision insurance applies in the conventional manner. However, it is the intent of the recent Quebec legislation that private insurers in the Province reach a "direct compensation" agreement whereby all payments for vehicle and property damage originate from the claimant's own insurer without regard to fault. The insurer can then subrogate the liability insurer to recover his payment if his policyholder is not at fault. The direct compensation approach would apply even in cases where the driver has no collision coverage.

It should be noted that compulsory vehicle damage insurance in the public ownership Provinces of Manitoba and Saskatchewan does not fall under no-fault. Government ownership does provide some of the same advantages as no-fault, because the majority of Manitoba and Saskatchewan residents are insured under the same company, that is by the provincial insurance corporation. As a result, disputes and subrogation among insurers are avoided. However these Provinces have not eliminated the right to sue for vehicle damage and for this reason they must still devote time and staff to the process of fault investigation.

British Columbia, the third government ownership Province, returned to an optional vehicle damage insurance system in 1976 after two years of experience under compulsory coverage. Discontent among many B.C. motorists who felt they were being forced to buy coverage that they did not want, and who complained about subsidizing high-risk drivers, contributed to the decision to revert to an optional coverage system. As in the other two government ownership Provinces, vehicle damage insurance is still under the fault system.

7. Property Other Than Vehicles and Contents

In order to safeguard owners of property other than vehicles and their contents, such as hydro poles, fences, buildings, etc., a no-fault approach also requires that every vehicle owner assume responsibility for damage to such property caused by his automobile, regardless of fault. Pure no-fault requires compulsory property protection insurance. High limits, of say \$1 million, are typically applied to this coverage.

The main objection advanced against this proposal is that it forces the vehicle owner and his insurance company to pay for another person's loss even if the vehicle owner is not at fault. On the opposing side is the argument that property owners should not be forced to rely on their own property insurance and incur higher rates because of an incident involving damage by an automobile. It is argued that the automobile should bear all losses caused by it, as it is an intrinsically dangerous thing which is nevertheless necessary to society.

Table 9 of Appendix A summarizes the types of coverages available in eleven selected plans to protect property other than vehicles and contents. Only three of the eleven plans require that a no-fault property protection coverage be purchased by every vehicle owner. Variplan, which places vehicle damage under the no-fault concept, retains other property damage under the liability system as part of the general residual liability insurance for both bodily injury and property damage.

8. Overview

Improved efficiency in the property damage component of automobile insurance will benefit both the motoring community and the individual motorist. It would appear that this objective can be advanced by the application of no-fault principles to property damage insurance. Under the no-fault system the claims settlement process can be simplified resulting in improved efficiency; the only unanswered question is the extent of this improvement.

To compensate for the situation wherein a blameless driver is left without the right to sue for recovery of his loss, the pure no-fault system proposes to make own vehicle damage insurance compulsory. Compulsory insurance ensures recovery of damages by all drivers, except for the deductible portion. Because the public appears to demand deductible recovery the concept of the fault deductible has been introduced.

Compulsory no-fault vehicle insurance, however, raises questions of affordability and of the justice of forcing an individual to protect his investment in his automobile. For these reasons, forms of limited collision coverage and methods of deductible recovery have been suggested as options either within a compulsory or within an elective property damage insurance system.

APPENDICES

Tables **APPENDIX A Details of Selected Plans or Proposals for No-Fault Coverage**

1. No-Fault Compensation for Bodily Injury:
 Medical, Hospital and Rehabilitative Expenses
2. No-Fault Compensation for Bodily Injury:
 Commentary on Medical Benefits in Selected Plans
3. No-Fault Compensation for Bodily Injury:
 Wage Loss Benefits for the Totally Disabled Wage-Earner
4. No-Fault Compensation for Bodily Injury:
 Wage Loss Benefits for the Partially Disabled or Non Wage-Earner
5. No-Fault Compensation for the Death of a Family Member
6. No-Fault Compensation for the Death of a Family Member:
 Details of Method of Payment of Earnings-Related Benefits
7. No-Fault Compensation for Bodily Injury:
 Benefits for Non-Economic Loss
8. Coverage for Loss or Damage to Own Vehicle
9. Property Protection Coverage (For Other Than Vehicles and Contents)
10. Coverages Basic to Selected Automobile Insurance Policies and Proposals

APPENDIX B Motor Vehicle Claims in the Courts

1. Province of Ontario—Motor Vehicle Claims in the Courts
2. Motor Vehicle Actions Compared to Total Civil Court Actions
3. Estimate of Court Time Spent on Motor Vehicle Cases
4. Civil Actions in Courts Across Canada (Excluding Ontario)

APPENDIX C Worksheets for Cost Calculations in Sections G and I

1. Worksheet (Table 11 and Table 12)
2. Worksheet (Table 13), 1973 Experience
3. Worksheet (Table 13), Pure No-Fault
4. Worksheet (Table 13), Mixed Fault/No-Fault
5. Worksheet (Table 13), Enriched Accident Benefits
6. Derivation of Cost Estimates for First-Party Benefit Enrichments in Tables 15, 16 and 17
7. Worksheet (Table 20), Apparent Distribution of Loss Costs for Property Damage

NO-FAULT COMPENSATION FOR BODILY INJURY
MEDICAL, HOSPITAL AND REHABILITATIVE EXPENSES

Current Or Proposed Plans	Dollar Limit	Time Limit	Long-Term Expense	Relationship to Other Insurance
Ontario (current)	\$5,000	4 years	No provision/OHIP coverage	Benefits not available if provided by other sickness or accident plans. These plans can subrogate.
Select Committee Proposal *	\$25,000	4 years	No provision	As above
Advocates Society Proposal	\$5,000	N/A	No provision	As above
J.B.M. Murray Proposal	Maximum subject to economic loss coverage: \$100,000 compulsory		No provision	As above
VARIPLAN - I.B.C. Proposal	\$20,000	N/A	No provision	As above
Michigan (current)	Unlimited		Unlimited	Government benefits are subtracted. No subrogation.
Proposed U.S. Standard	\$100,000 or 2 years	Optional 2 years	No provision	Government benefits are subtracted. No subrogation.
New Zealand (current)	Unlimited		Unlimited	Benefits are in excess of coverage under Social Security Act. No subrogation.
Saskatchewan Proposal	Unlimited		Unlimited	Benefits are in excess of provincial health plan. No subrogation.
Quebec (New Legislation)	Unlimited		Unlimited	Benefits are in excess of public health insurance. No subrogation.
Ontario Law Reform Commission	Unlimited		Unlimited	As in Ontario (current).

* Effective July 1, 1978

**NO-FAULT COMPENSATION FOR BODILY INJURY
COMMENTARY ON MEDICAL BENEFITS
IN SELECTED PLANS**

A. ONTARIO (CURRENT)

All necessary medical, surgical, dental, hospital, professional nursing, and ambulance service. All other services and supplies deemed essential by the attending physician and Insurer's medical advisor, for treatment or rehabilitation.

B. ONTARIO (PROPOSED)*

All reasonable expenses incurred within four years from the date of the accident as a result of such injury for necessary medical, surgical, dental, chiropractic, hospital, professional nursing and ambulance service and for any other service within the meaning of insured services under *The Health Insurance Act* and for such other services and supplies which are, in the opinion of the physician of the insured person's choice and that of the Insurer's medical advisor, essential for the treatment, occupational retraining or rehabilitation of said person.

C. MICHIGAN

Allowable expenses not in excess of customary charge for semi-private accommodation, except for intensive care. All reasonable charges for reasonably necessary products, services, accommodations for an injured person's care, recovery or rehabilitation.

D. QUEBEC (NEW LEGISLATION)

The victim is entitled, in every case, without limit of time and to the extent that they are not already covered by a social security scheme, to the reimbursement of reasonable expenses incurred by reason of an accident for medical and paramedical care, transportation by ambulance or other means for the purpose of receiving such care, the purchase of prostheses or orthopedic devices and the replacement of clothing. The victim is also entitled to the reimbursement of such other expenses of a similar nature as may be authorized by the Regie.

E. SASKATCHEWAN (PROPOSED)

All reasonable expenses including dental work, nursing care, ambulance service, physiotherapy, and any other service, supplies or treatment needed for successful treatment of the injuries.

F. ONTARIO LAW REFORM COMMISSION

1. All reasonable expenses, for necessary medical, surgical, dental, hospital, professional nursing and ambulance services, and all reasonable costs of drugs, and other supplies and equipment essential to the treatment of the injured person.
2. All services, including psychiatric, psychological and other support services, physical and occupational therapy, including job retraining if necessary for the maximum physical, emotional, social and vocational rehabilitation of the injured person.

G. U.S. PROPOSED NATIONAL STANDARD

Insurers must make available optional coverages up to \$1 million in medical benefits. State no-fault plans must provide for an impartial mechanism to establish guidelines for the evaluation and supervision of medical care, emergency medical services, and rehabilitation services.

* Effective July 1, 1978

NO-FAULT COMPENSATION FOR BODILY INJURY
WAGE-LOSS BENEFITS FOR THE TOTALLY
DISABLED WAGE-EARNER

Current or Proposed Plans	Maximum Earnings Eligible for Compensation (Annual)	Rate of Payment as Percent of Earnings	Maximum Net Benefit Per Week	Minimum Net Benefit Per Week	Period of Eligibility	Waiting Period or Deductible
Ontario (current)	\$4,550	80%	\$ 70.00	none	2 years	none
Select Committee Proposal *	\$9,100	80%	\$140.00	none	2 years	none
Advocates Society Proposal	\$7,735	80%	\$119.00	none	unlimited	none
J.B.M. Murray Proposal	Actual income, subject to limit of coverage: \$100,000, compulsory coverage; higher limits are voluntary					
VARIPLAN - I.B.C. Proposal	\$13,000	80%	\$200.00	none	3 years	7 days
Michigan (current)	\$19,384	85%	\$343.25	none	3 years	none
Proposed U.S. Standard	\$13,000	actual	\$250.00	none	1 year	7 days or \$200
New Zealand (current)	\$15,600	80%; 90% for low earners	\$240.00	\$48.00 net	unlimited	7 days
Saskatchewan Proposal	\$10,000	net of tax	\$187.50	\$30.00 net	5 years	none
Québec (New Legislation)	\$18,000	90% of net after tax	\$300.00	\$80.00, plus \$10 per dependant up to \$120.00	5 years	7 days
Ontario Law Reform Commission	\$16,250	80%	\$250.00	none	unlimited	none

* Effective July 1, 1978

NO-FAULT COMPENSATION FOR BODILY INJURY
WAGE LOSS BENEFITS FOR THE PARTIALLY
DISABLED OR NON-WAGE-EARNERS

Current or Proposed Plans	Partially Disabled Earner	Unemployed	Student or Minor	Homemaker or Spouse	Over 65 at time of Accident
Ontario (current)	No provision	No provision	No provision	\$35/wk. for 12 weeks if completely incapacitated	Earners' benefits if employed; otherwise no provision
Select Committee Proposal *	No provision	No provision	No provision	\$70/wk. for 12 weeks if completely incapacitated	As above
Advocates Society Proposal	No provision	No provision	No provision	\$80/wk. for 12 weeks if completely incapacitated	No provision
-----Unspecified-----					
I.B.M. Murray Proposal	Any income earned reduces benefit payable for compensation	No provision	No provision	Up to \$20/day for 3 years for replacement services hired, 7-day waiting period.	As in Ontario today
WALPLAN - I.B.C. Proposal	Benefits added to any income earned not to exceed maximum for total disability	Benefit based on earned income for last month fully employed	No provision	Up to \$20/day for 3 years for replacement services hired	As above
Michigan (current)	Benefits added to any income earned not to exceed maximum for total disability	Benefit based on probable weekly income	No provision	Up to \$20/day payable for 365 days	No apparent provision
Proposed U.S. Standard	No apparent provision	Payment based on probable weekly income	No apparent provision	Any expense or loss incurred by another person in giving help to injured person is reimbursed. No other apparent provision	Earners' benefits payable for 5 years. If accident occurs between ages 60-65; until age 70 if between ages 65-69; one year, after age 69
New Zealand (current)	Any income earned reduces benefit payable for compensation	Earners' coverage granted for period up to 13 weeks, if person employed some time in year prior to accident	\$18/wk. to \$72/wk. net (\$40-\$120 gross); payable age 16 and over	Lesser of \$187.50/wk. or reasonable costs of a domestic servant, even if not hired; 5 year limit	Benefits adjusted at age 65 to ensure income is maintained at 2/3 of net earnings at date of accident. 2 years full benefits paid to those injured after age 65.
Saskatchewan Proposal	As above	Earnings at last place of employment	\$30/wk. if 10-15 yrs; \$75/wk. if 15-18 yrs; \$150/wk., if over 18	As under unemployed; or expenses up to \$150/wk., or \$80/wk., for children under 18	If able to work, appropriate indemnity paid for: (a) 5 years, age 65-70; (b) 1 year, age 71-75; (c) 1 year max., age over 75
Dubuec (New Legislation)	Total disability payment reduced by 50% of first \$9,000 of net income, and 7% of remainder	Based on presumptive income evaluated on prospects for employment	Avg. weekly industrial wage in Quebec; \$80/wk. for children under 18	Income evaluated on prospects for employment	Income evaluated on prospects for employment
Ontario Law Reform Commission	Payments reduced as earning capacity is regained	Payment based on probable weekly income	Income evaluated on prospects for employment, modest adjustment to reflect warning potential	Income evaluated on prospects for employment	Income evaluated on prospects for employment

* Effective July 1, 1978

NO-FAULT COMPENSATION FOR THE DEATH
OF A FAMILY MEMBER

Current or Proposed Plans	Method of Payment	Funeral Expenses	Death of Spouse or Parent Contributing to Family Income			Death of Spouse Not Contributing to Family Income	Benefits to Parents on Death of Children
			Principal Benefit	Additional Each	Total Limit		
Ontario (current)	Fixed sum	\$500	\$5,000	\$1,000	none	\$2,500	\$500 under 5 yrs; \$1,000 for 5-10 yrs; nil, for 21 and over
Select Committee Proposal **	Fixed sum	\$1,000	\$10,000	\$1,000	none	\$10,000	\$1,000 under 5 yrs; \$2,000 for 5 yrs and over
Advocates Society Proposal	Fixed sum	\$1,000	\$5,000	\$1,000	none	\$5,000	As in current Ontario plan
-----Unspecified Separate Coverage-----							
J.B.M. Murray Proposal							
VARIPLAN - I.B.C. Proposal	Fixed sum	\$1,000	\$5,000	\$1,000	none	\$5,000	\$1,000 under 18 yrs; Nil, for 18 yrs. and over
Michigan (current)	Earnings related	Included in Principal Benefit	-----\$12,000* for 3 years-----			\$20/day for 3 years replacement services	Nil
Proposed U.S. Standard	Fixed sum		\$1,000; insurers required to make available optional coverages with extra benefits				
New Zealand (current)	Fixed sum, plus earnings related	Actual and reasonable expenses	\$1,000 plus \$7,800*	\$500 plus \$2,600*	\$1,500 plus \$7,800*	Any quantifiable loss of service, proven to have been suffered, or coverage under supplementary plan	
Saskatchewan Proposal	Fixed sum, plus earnings related	\$1,000	\$7,500 plus \$4,500*	\$1,500*	\$4,500*	\$7,500, plus cost of replacing services	\$750 under 5 years; \$1,500 for 6-10 years; \$2,250 for 11-15 years; \$1,000 for 16 years and over
Quebec (New Legislation)	Earnings related	\$1,000	\$9,900*	\$900 to \$1,800*	\$4,500*	As for unemployed. Min. \$80/wk., plus \$10/dependent up to \$120/wk.	
Ontario Law Reform Commission	Fixed sum, plus earnings related	\$1,000	\$1,000 plus \$12,000*	\$1,000*	\$6,000* incl. in principal benefit	\$1,000	As in current Ontario plan

* Earnings-related benefits: amount indicates maximum
wage (at gross value) payable per year.

** Effective July 1, 1978 with adjustments

(Refer to AppendixH of the Committee's Second Report.)

NO-FAULT COMPENSATION FOR THE DEATH OF A
FAMILY MEMBER
DETAILS OF METHOD OF PAYMENT OF
EARNINGS-RELATED BENEFITS

A. MICHIGAN (CURRENT)

Benefits payable for loss of contributions that dependants would have received from the deceased for support during their dependency. Also \$20/day allowance for replacing services provided by the deceased (proof of purchase required). Benefits not to exceed \$1,000 in a single 30-day period, and not payable beyond first 3 years.

B. QUEBEC (NEW LEGISLATION)

- a) Weekly payment of 55% of net income of head, subject to gross income maximum of \$18,000/yr., for first dependant.
- b) 10% of net income of head for next dependant, and 5% for each other, to a maximum of 80% of net income of head.
- c) Minimum of \$80/wk., plus \$10 per child, up to \$120/wk.
- d) 1 week waiting period. No time limit specified.

C. SASKATCHEWAN (PROPOSED)

- a) \$7,500 fixed sum.
- b) For surviving spouse, or next dependant on death of both parents: 50% of disability income entitlement of deceased, subject to net disability income maximum of \$9,000/yr.; for 5 years or until remarriage, or for length of dependency if a child.
- c) For additional dependants (including dependent parents): 1/6 of disability income for each other dependant, not to exceed 100% of entitlement, continued for length of dependency.
- d) A retaining allowance is available for spouse not working at time of earner's death.

D. NEW ZEALAND

- a) \$1,000 fixed sum in case of total dependence by spouse; \$500 for children.
- b) On death of an earner, totally dependent spouse receives 50% of disability income entitlement of deceased, subject to a net disability income

maximum of N.Z. \$12,480/yr. Payment ceases on remarriage, with "gift" of a lump sum equivalent to two years' benefit. Payment reduced for partial dependence.

- c) Totally dependent children receive 1/6 of disability income entitlement, or 1/3 if orphaned.
- d) Other dependants compensated at discretion of Commission.

E. ONTARIO LAW REFORM COMMISSION

- a) Remaining spouse or dependants to receive monthly allowance, based on actual loss of contributions to family income, but not to exceed \$1,000 (gross) per month.
- b) A widow remarrying receives 1 year's payments in lump sum. Children's benefits remain, but at 50% of family income loss. Adjustments to be made as children reach majority or leave school.

NO-FAULT COMPENSATION FOR BODILY INJURY
BENEFITS FOR NON-ECONOMIC LOSS

Current or Proposed Plans	Indemnity for Dismemberment, Pain and Inconvenience
Ontario (current) Select Committee Proposal Advocates Society Proposal J.B.M. Murray Proposal VARIPLAN—I.B.C. Proposal Michigan (current) Proposed U.S. Standard New Zealand (current) Quebec (New Legislation) Ontario Law Reform Commission	Recovery from Negligent Third-Party As above As above As above As above As above, in case of serious injury As above, in case of serious injury No-fault payment No-fault payment No recovery

Details of No-Fault Payments

A. NEW ZEALAND

- a) \$7,000 lump sum for permanent loss or impairment of any bodily function, or loss of any bodily function, or loss of any part of the body.
- b) A percentage of \$7,000 for partial loss or other impairments.
- c) \$10,000 maximum lump sum in respect of: (i) the loss suffered by the person of amenities or capacity for enjoying life, including loss from disfigurement; and (ii) pain and mental suffering including nervous shock and neurosis.

B. SASKATCHEWAN

\$15,000 maximum lump sum in case of mutilation. Percentage of \$15,000 based on indemnity tables.

C. QUEBEC

\$20,000 or a percentage based on indemnity tables or determined by Regie. Available to all persons suffering defined loss.

COVERAGE FOR LOSS OF OR DAMAGE TO OWN VEHICLE

APPENDIX A
Table 8

CURRENT OR PROPOSED PLANS	GENERAL PROVISION			A. RECOVERY FOR VEHICLE REPAIRS OR LOSS: DRIVER AT FAULT			B. RECOVERY FOR VEHICLE REPAIRS OR LOSS: DRIVER NOT AT FAULT			C. RECOVERY FOR LOSS OF USE	D. RECOVERY FOR LOSS OF CONTENTS
	Coverage	Type of Coverage	Deductible	Coverage Bought	Deductible Portion	No Coverage Bought	Coverage Bought	Deductible Portion	No Coverage Bought		
ONTARIO (CURRENT)	Optional	1. Collision or Upset 2. Comprehensive 3. Specified Perils 4. All Perils	Usual deductibles: \$25, \$50, \$100, \$250.	Own insurer pays.	No recovery.	No recovery.	Own insurer pays; can subrogate.	Subrogate party at fault.	Subrogate party at fault.	In case of theft - \$8/day, max. \$40. Otherwise, subject to deductible and rules of recovery.	Available, subject to deductible and rules of recovery.
SELECT COMMITTEE PROPOSAL	Optional	1. Collision or Upset 2. Comprehensive (other than collision, including specified perils)	Standard minimum: \$250.	Own insurer pays.	No recovery.	No recovery.	Own insurer pays; can subrogate.	Subrogate party at fault.	Subrogate party at fault.	In case of theft - \$12/day, max. \$360. Otherwise, subject to deductible and rules of recovery.	Available, subject to deductible and rules of recovery.
ADVOCATES SOCIETY PROPOSAL	Optional	As in Ontario (Current)	As in Ontario (Current)	Own insurer pays.	No recovery.	No recovery.	Own insurer pays; can subrogate.	Subrogate party at fault.	Subrogate party at fault.	As in Ontario (Current).	As in Ontario (Current).
J.B.N. HURRY PROPOSAL	Compulsory No-fault	Damage coverage for Collision and Comprehensive included in compulsory First Party Economic Loss Section (which includes bodily injury coverage).	\$500 fault deductible. No buy-back. Larger deductibles (not based on fault) can be bought at choice of insured.	Own insurer pays.	No recovery.	Must have coverage.	Own insurer pays; no subrogation within compulsory \$100,000 limit. If residual exists, right of subrogation remains).	Own insurer pays \$500 fault deductible. No subrogation. No recovery if higher deductibles are purchased.	Must have coverage.	Receipts required. Fully covered if total costs within limits of plan, subject to deductible.	Proof of worth required. Fully covered if total costs within limits of plan, subject to deductible.
VARIPLAN - I.B.C. PROPOSAL	Optional No-fault	1. Collision Plans A,B,C. 2. Comprehensive 3. Specified Perils 4. All Perils	Standard Deductible for A and B: \$100 or \$250 Heavy vehicles: Standard Deductible for C: \$50 or \$100 for heavy vehicles.	Plan A - Own insurer pays. Plan B - Own insurer pays. Plan C - No recovery.	Plan A - No recovery. Plan B - No recovery. Plan C - No recovery.	Plan A - No recovery. Plan B - No recovery. Plan C - No recovery.	Plan A - Own insurer pays; no subrogation. Plan B - Own insurer pays; no subrogation. Plan C - Own insurer pays 100% or 50%, based on Recovery Rules. No subrogation.	Plan A - Own insurer pays either 50% or 100% based on Recovery rules; no subrogation. Plan B - Own insurer pays in one case only, when car is struck while parked; otherwise, no recovery. Plan C - No deductible if driver is 100% not at fault. Deductible applied (no recovery) if driver 50% at fault.	Plan A - No recovery. Plan B - No recovery. Plan C - No recovery.	Maximum of \$10/day, up to 15 days. Deductible does not apply to loss of use. No right to subrogate.	None. Separate endorsement required. No right to subrogate.
MICHIGAN (CURRENT)	Optional No-fault	1. Collision, various coverages 2. Comprehensive 3. All Perils	No standard specified. Various deductibles offered including a waiver of deductible.	Own insurer pays.	No recovery (unless extended coverage is bought).	No recovery.	Own insurer pays; no subrogation.	No recovery (unless extended coverage is bought).	No recovery.	Receipts required. Subject to deductible and rules of recovery.	Available, subject to deductible and rules of recovery.
PROPOSED U.S. STANDARD		Individual States are free to set own guidelines.									
NEW ZEALAND (CURRENT)	Optional	1. Collision and Upset 2. All risks	Details unknown.	Own insurer pays.	No recovery.	No recovery.	Own insurer pays; no subrogation.	No recovery.	No recovery.	Unknown.	Unknown.
SASKATCHEWAN PROPOSAL	Compulsory No-fault	Comprehensive (including collision and all risks)	\$200 standard deductible.	Own insurer pays.	No recovery.	Must have coverage.	Own insurer pays; no subrogation.	No recovery.	Must have coverage.	Receipts required. Subject to deductible and rules of recovery.	Not specified. Presumably available.
QUERY (AND LEGISLATION)	Optional	As in Ontario (Current)	No standard specified.	Own insurer pays.	No recovery.	No recovery.	Own insurer pays; can subrogate.	Own insurer pays; can subrogate.	Own insurer to pay and then subrog. (or, litigation)	Receipts required. Subject to deductible and rules of recovery.	Not specified. Presumably available.
ONTARIO LAW REFORM COMMISSION PROPOSAL	Optional No-fault	1. Collision 2. All risks	No standard specified.	Own insurer pays.	No recovery.	No recovery.	Own insurer pays; no subrogation.	No recovery.	No recovery.	Available. No details.	Not specified. Presumably available.

PROPERTY PROTECTION COVERAGE
(For other than vehicles and contents)

CURRENT OR PROPOSED PLANS	TYPE OF COVERAGE APPLICABLE	COVERAGE	MINIMUM STANDARD LIMIT	IS THERE PRIORITY FOR BODILY INJURY UNDER THIS COVERAGE?	WHO CAN RECOVER? PARTY AT FAULT PARTY NOT AT FAULT	MEANS OF RECOVERY
ONTARIO (CURRENT)	Residual Liability Insurance for Bodily Injury and Property Damage	Not Compulsory	\$100,000	Yes	No	Subrogation of party at fault.
SELECT COMMITTEE PROPOSAL	As above	Compulsory	Unlimited	Yes	No	Subrogation of party at fault.
ADVOCATES SOCIETY PROPOSAL	As above	Compulsory	\$100,000 or more	Yes	No	Subrogation of party at fault.
J.B.M. MURRAY PROPOSAL	As above.	Compulsory	\$1 million or unlimited	Yes	No	Subrogation of party at fault.
VARIPLAN - I.B.C. PROPOSAL	As above	Compulsory	\$100,000 or more	Yes	No	Subrogation of party at fault.
MICHIGAN (CURRENT)	a) Property Protection Insurance (for accidents in the State) - excludes property owned by insured or relatives. b) Residual Liability Insurance for Bodily Injury and Property Damage (for accidents outside the State).	Compulsory	\$1,000,000	No	Yes	Insurer of vehicle that damaged property is absolutely liable regardless of fault.
PROPOSED U.S. STANDARD	Individual States are free to set own Guidelines	Compulsory	\$20,000	Yes	No	Subrogation of party at fault.
NEW ZEALAND (CURRENT)	Liability Insurance for Property Damage	Compulsory	Details Unknown	No	No	Subrogation of party at fault.
SASKATCHEWAN PROPOSAL	Liability Insurance for Property Damage	Compulsory	\$50,000	No	Yes	Insurer of vehicle that damaged property is absolutely liable regardless of fault.
QUEBEC (NEW LEGISLATION)	Liability Insurance for Bodily Injury and Property Damage	Compulsory	\$50,000	No	Yes	Subrogation of party at fault
ONTARIO LAW REFORM COMMISSION	Liability Insurance for Property Damage	Compulsory	To be determined on basis of underwriting experience.	No	Yes	Insurer of vehicle that damaged property is absolutely liable regardless of fault.

CURRENT OR PROPOSED PLANS	1. ACCIDENT BENEFITS COVERAGE				2. OWN VEHICLE DAMAGE COVER		
	Underwriter	Compulsory	Claimant	Rating	Underwriter	Compulsory	Claimant
ONTARIO (CURRENT)	Private	Compulsory ⁽¹⁾	Insured	Flat-rated.	Private	Optional	Insured. Third-party for deductible if insured at fault.
SELECT COMMITTEE PROPOSAL	Private	Compulsory	Insured	Flat-rated.	Private	Optional	Insured. Third-party for deductible if insured at fault.
ADVOCATES SOCIETY PROPOSAL	Private	Compulsory	Insured	Flat-rated.	Private	Optional	As in Ontario
J.B.M. MURRAY PROPOSAL	Private	Compulsory	Insured	Class-rated; no merit rating.	Combined with Accident Benefits in First- Loss Coverage.		
VARIPLAN-I.B.C. PROPOSAL	Private	Compulsory	Insured	Four-class rating; no merit rating.	Private	Optional	Insured
MICHIGAN (CURRENT)	Private	Compulsory	Insured	Flat-rated.	Private	Optional	Insured
PROPOSED U.S. STANDARD	Private	Compulsory	Insured	Not specified.	Private	Optional	As in Ontario
NEW ZEALAND (CURRENT)	Public	Compulsory	Insured	Flat fee, included with vehicle licence fee	Private	Optional	Insured
SASKATCHEWAN PROPOSAL	Public	Compulsory	Insured	Flat-rated. Included with vehicle licence fee	Public	Compulsory	Insured
QUEBEC (NEW LEGISLATION)	Public	Compulsory	Insured	Flat fee, included with vehicle licence fee	Private	Optional	As in Ontario
ONTARIO LAW REFORM COMMISSION PROPOSAL	No Recommendation	Compulsory	Insured	Flat-rated.	No Recommendation	Optional	Insured

(1) Compulsory only if Liability Coverage is purchased.

(2) Liability Insurance for Bodily Injury applicable only out-of-province.

ED
PROPOSALS

APPENDIX A
Table 10

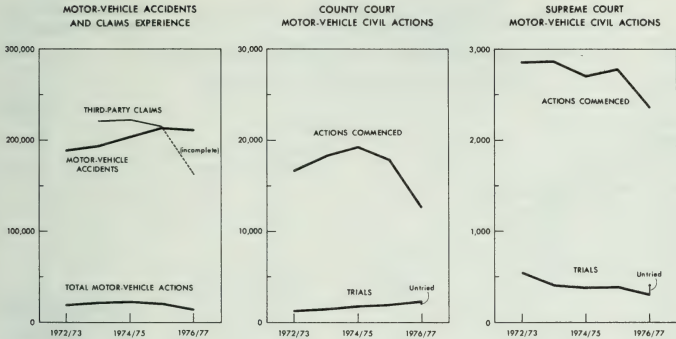
BODILY INJURY AND PROPERTY DAMAGE LIABILITY COVERAGE FOR BODILY INJURY AND			4. OTHER BASIC COVERAGE				
Compulsory	Claimant	Rating	Type	Underwriter	Compulsory	Claimant	Rating
Optional	Third-party, if insured at fault.	Class-rated; Merit-rated.					
Compulsory	Third-party, if insured at fault.	Class-rated; Merit-rated.					
Compulsory	Third-party, if insured at fault.	Class-rated; Merit-rated.					
Compulsory	Third-party, if insured at fault.	Class-rated; Merit-rating based on number of chargeable accidents in last 7 years.	Accident Death and Dismemberment Coverage	Private	Optional	Insured (or family)	Flat-rated, by level of coverage.
Compulsory	Third-party, if insured at fault - subject to threshold.	Class-rated; no merit rating.					
Compulsory	Third-party, if insured at fault - subject to threshold.	Class-rated; Merit-rated.	Property Protection Coverage (non-vehicle)	Private	Compulsory	Third-party, regardless of fault.	Flat-rated.
Compulsory	Third-party, if insured at fault - subject to threshold.	Not specified.					
			Liability Coverage for Property Damage	Private	Compulsory	Third-party, regardless of fault.	Not known.
			Liability Coverage for Property Damage	Public	Compulsory	Third-party, regardless of fault.	Not known.
Compulsory	Third-party, if insured at fault. (2)	Class-rated; Merit-rated					
			Liability Coverage for Property Damage	No Recommendation	Compulsory	Third-party, regardless of fault.	Not known.

APPENDIX B

MOTOR VEHICLE CLAIMS IN THE COURTS

APPENDIX B
Table 1

PROVINCE OF ONTARIO — MOTOR-VEHICLE CLAIMS IN THE COURTS



SOURCE: Insurance Bureau of Canada
Ministry of Transportation and Communications
Ministry of the Attorney General

APPENDIX B
Table 2

MOTOR-VEHICLE ACTIONS COMPARED TO TOTAL CIVIL COURT ACTIONS PROVINCE OF ONTARIO, 1976/77

	Actions Commenced		Actions Tried	
<i>Supreme Court</i>				
Motor-Vehicle	2,354	6%	310	2%
Divorce	22,178	51	20,791	94
Other	18,770	43	902	4
Total	<u>43,302</u>	<u>100%</u>	<u>22,003</u>	<u>100%</u>
<i>County Court</i>				
Motor-Vehicle	12,609	18%	2,276	53%
Other	58,538	82	2,022	47
Total	<u>71,147</u>	<u>100%</u>	<u>4,298</u>	<u>100%</u>
<i>Total</i>				
Motor-Vehicle	14,963	13%	2,586	10%
Divorce	22,178	19	20,791	79
Other	77,308	68	2,924	11
Total	<u>114,449</u>	<u>100%</u>	<u>26,301</u>	<u>100%</u>

Source: Ministry of the Attorney General.

APPENDIX B
Table 3

ESTIMATE OF COURT TIME SPENT ON
MOTOR-VEHICLE CASES
PROVINCE OF ONTARIO, 1976/77

Distribution of Half Days Spent in Court by the Court Clerk

	Supreme Court October/76-March/77		County Court (excluding York County) April/76-September/76
Criminal	19%	Criminal	46%
Civil	46	Civil	42
Divorce	35	Other	11
	100%		100%
Estimate of Time Spent on Motor Vehicle Cases	12%	Estimate of Time Spent on Motor Vehicle Cases	22%

Source: Ministry of the Attorney General.

APPENDIX B
Table 4

CIVIL ACTIONS IN COURTS
ACROSS CANADA (EXCLUDING ONTARIO)
1971 Sample Survey

	Total Civil Actions %	Motor Vehicle Tort Actions %
<i>1. Duration of Civil Action</i>		
Less than 3 months	54.3	8.5
3 to 6 months	15.0	13.2
6 months to 1 year	14.1	26.4
1 to 2 years	11.3	34.0
2 years or more	5.3	17.9
Total	100.0	100.0
Number in Survey	6,565	750
<i>2. Results of Civil Action</i>		
For plaintiff	79.9	53.5
Discontinuance	18.0	41.4
For defendant	1.8	4.1
Decision for both	0.3	1.0
Total	100.0	100.0
Number in Survey	6,507	613

Source: *Perspective Canada II*, Statistics Canada, 1977

APPENDIX C

WORKSHEETS FOR COST CALCULATIONS IN SECTIONS G AND I

APPENDIX C
Table 1

WORKSHEET (TABLE 11 AND TABLE 12)
I.B.C. NO-FAULT STUDY
COMPARISON OF FUTURE AND PRESENT COSTS
All Types of Cars—Any Number per Accident
Four Provinces
Present Cost Data

				Exhibit 17 Sheet 2
				\$1.00 Equal to Net Benefits Received
				\$1.00 Equal to Total Benefits Paid by Industry
				Selected Claims (\$000)
BODILY INJURY & PASSENGER HAZARD				
<i>Claims</i>				
(1) Special damages	Net Benefits	(1,975	
(2) General damages	Received	(6,084	\$0.84
(3) Subrogation		(693	
(4) Plaintiff solicitor	Legal Costs	(845	<u>0.16</u>
(5) Total Claims				
(1) . . . (4)			9,598	\$1.00
<i>Expenses</i>				
(6) Legal	Claim	(770	
(7) Indep. Adj.	Adjusting	(367	
(8) Other	Costs	(82	
(9) Total expenses				
(6) . . . (8)			<u>1,219</u>	\$0.13

Source: Insurance Bureau of Canada, *No-Fault Study*, June 5, 1974, carried out by Woodward and Fondiller.

WORKSHEET (TABLE 13)
1973 Experience
I.B.C. NO-FAULT STUDY
COMPARISON OF FUTURE AND PRESENT COSTS
All Types of Cars—Any Number per Accident
Four Provinces
Present Cost Data

			Exhibit 17 Sheet 2
			Percent of Total Claims
BODILY INJURY & PASSENGER HAZARD			
<i>Claims</i>			
(1) Special damages		1,975	
(2) General damages		6,084	
(3) Subrogation		(693)	
(4) Plaintiff solicitor	Legal Costs	(845)	16.0%
(5) Total claims (1) . . . (4)		9,598	
<i>Expenses</i>			
(6) Legal		(770)	
(7) Indep. Adj.	Claim Adjusting Costs	(367)	
(8) Other		(82)	
(9) Total expenses (6) . . . (8)		1,219	12.7%

Source: Insurance Bureau of Canada, *No-Fault Study*, 1974.

WORKSHEET (TABLE 13)
Pure No-Fault
I.B.C. NO-FAULT STUDY
COMPARISON OF FUTURE AND PRESENT COSTS
All Types of Cars—Any Number per Accident
Four Provinces
Present Cost Data

				Exhibit 17 Sheet 2
				Percent of Benefits Paid
BODILY INJURY & PASSENGER HAZARD				
<i>Claims</i> (Adjustment made under Pure No-Fault)				
(1) Special damages		1,975		
(2) General damages		6,084		
(3) Subrogation	Legal Costs (Eliminated)	(693		Nil
(4) Plaintiff solicitor		(845		
(5) Total claims	(Total available for			
(1) . . . (4)	No-Fault Benefits)	9,598	9,598	100%
<i>Expenses</i>				
(6) Legal	(Eliminated)	770	—	
(7) Indep. Adj.	(+ 40% for extra staff adjusters)*	367	514	
(8) Other	(same)	82	82	
(9) Total expenses				
(6) . . . (8)		1,219	596	6.2%

* I.B.C. Study estimate.

Source: Insurance Bureau of Canada, *No-Fault Study*, 1974.

WORKSHEET (TABLE 13)
Mixed Fault/No-Fault
I.B.C. NO-FAULT STUDY
COMPARISON OF FUTURE AND PRESENT COSTS
All Types of Cars—Any Number per Accident
Four Provinces
Future Cost Data
(Describes the VARIPLAN Mixed Fault/No-Fault System)

Exhibit 17
Sheet 1

NO-FAULT COSTS		Selected Claims (\$000)	
(1) Fatal cases: Head hhld.		354	
(2) Fatal cases: Spouse		108	
(3) Fatal cases: Others		89	
(4) Fatal cases: Deps. after 1st		60	
(5) Fatal cases: Total		611	
(6) Wage loss benefits		1,331	
(7) Replacement services and subst. help		36	
(8) Medical		759	
(9) Total no-fault benefits (5) . . . (8)		2,737	
(10) Expenses at 7.5% of benefits*		205	
(11) Total no-fault cost (9) + (10)		2,942	
RESIDUAL LIABILITY			
(12) Pain and suffering		1,708	
(13) Permanent disability		83	
(14) Other general damages		483	
(15) Plaintiff solicitor		336	
(16) Subrogation		348	
(17) Excess of economic loss over no-fault benefits		169	
(18) Total residual claim (12) . . . (17)		3,127	
(19) Expenses @ 10% of (18)*		313	
(20) Total residual liability (18) + (19)		3,440	
			Percent of Total Benefits
Total Benefits (9) + (18)		5,864	
Total Claims Adjusting Costs (10) + (19)		518	8.8%
Total Legal Costs (15) + (16)		684	11.7%

* I.B.C. Study Estimate

Source: Insurance Bureau of Canada, *No-Fault Study*, 1974.

WORKSHEET (TABLE 13)
Enriched Accident Benefits
I.B.C. NO-FAULT STUDY
COMPARISON OF FUTURE AND PRESENT COSTS
All Types of Cars—Any Number per Accident
Four Provinces
Present Cost Data

		Selected Claims (\$000)	Enriched Benefits (\$000)	Percent of Benefits Paid
BODILY INJURY & PASSENGER HAZARD				
<i>Claims (Adjustments)</i>				
(1) Special damages	(Same)	1,975	1,975	
(2) General damages	(Same)	6,084	6,084	
(3) Subrogation	(Reduced by 25%)*	693	520)	12.5%
(4) Plaintiff solicitor	(Reduced by 25%)*	845	634)	
(5) Total Claims (1) . . . (4)		<u>9,598</u>	<u>9,213</u>	100%
<i>Expenses</i>				
(6) Legal	(Reduced by 25%)*	770	578	
(7) Indep. Adj.	(Same)	367	367	
(8) Other	(Same)	82	82	
(9) Total expenses (6) . . . (8)		<u>1,219</u>	<u>1,027</u>	11.1%

* 25% = (1) ÷ ((1) + (2))

Source: Insurance Bureau of Canada, *No-Fault Study*, 1974.

**DERIVATION OF COST ESTIMATES FOR
FIRST PARTY BENEFIT ENRICHMENTS IN
TABLES 15, 16 AND 17**

Adjustment A: Quadruple Weekly Indemnity Limit

- Increase maximum wage loss benefits from \$70/week* to \$280/week.
- Net indemnity to be paid at 85% of gross wage value, subject to above maximum.
- Assume average recovery is at the level of the average industrial wage in Ontario (\$252.00 per week in June 1977).
- At net equal to 85%, average recovery will amount to roughly \$215/week or \$11,180 per year.
- Assume initially the same claim frequency (see last assumption) and the same period of eligibility (2 years) as at the present time.
- Assume current indemnity is virtually all paid out at \$70/week.* Therefore raising limits increases average payments from \$70/week to \$215/week or about three times.
- Current total cost of wage indemnity is \$18 million (including claim settlement costs that are disregarded). A threefold increase in average payments would increase total costs to \$54 million.
- Assume that claims frequency increases by 20% as first-party wage loss limits are increased. The total cost of benefits will therefore increase by 20% from \$54 million to \$65 million.

Adjustment B: Provision for Permanent Disability

- Assume that the number of large claims paid by insurers approximates the number of persons seriously or permanently disabled as a result of automobile accidents.
- Assume that about 100 injuries per year result in long-term disability based on 1975 I.B.C. data indicating that some 90 persons incurred losses over \$100,000.
- Assume that long-term claims are paid out for an average of 16.62 years as developed in the I.B.C. *No-Fault Study*, Exhibit 16, page 37.
- Payments are made at the level provided in Adjustment A.

— The calculation of Benefits paid under the permanent disability adjustment is illustrated below:

(1) Average weekly indemnity, net	\$215
(2) Annual benefit @ 52 weeks	\$11,180
(3) Average life expectancy of totally disabled	16.62 years
(4) Present value of benefits per claimant (2) × (3)	\$185,812
(5) Total cost of 100 cases in a typical year	\$18,581,200

— No factor is added for claim settlement costs.

Adjustment C: Provision for Death Benefits on an Earnings-Related Basis

— Assume payments made to dependants would continue for four years.

— The average annual payment is assumed to be \$11,180 as in Adjustment A.

— The number of motor vehicle fatalities per year in Ontario is currently about 1,500.

— Because 46% of persons killed in 1976 were under 25 years of age and likely left no dependants, assume only about 55% of victims killed in automobile accidents leave dependants who require death benefits.

— Calculation of the death benefits paid is illustrated below:

(1) Average weekly indemnity, net	\$215
(2) Annual benefit	\$11,180
(3) Period of payment	4 years
(4) Present value of benefits per claimant (2) × (3)	\$44,720
(5) Number of claimants per year (55% of 1,500)	825
(6) Total cost (4) × (5)	\$36,894,000

— No factor is added for claim settlement costs.

* Effective July 1, 1978, the maximum payable for loss of earnings doubles to \$140 per week.

WORKSHEET (TABLE 20)
APPARENT DISTRIBUTION OF
LOSS COSTS FOR PROPERTY DAMAGE

1. DATA BASED ON 1975 LOSSES INCURRED IN ONTARIO

Property Damage Coverage	Losses (\$ million)	Claims	Drivers Insured (millions)	Approx. Claims Frequency
Liability (actual)	\$121	190,000	2.750	.069
Collision (actual)	\$117	180,000	2.075	.087
Liability but not Collision (25% of owners)	—	47,500	.675	.070
Liability and Collision (75% of owners)	—	142,500	2.075	.069

Source: Insurance Bureau of Canada, *Automobile Insurance Experience*, 1976. (Green Book)

2. AVERAGE DEDUCTIBLE ON COLLISION COVERAGE—CANADA-WIDE EXPERIENCE, 1975

Deductibles	Insured	%	% × Deductible Amount
\$ 25	32,092	.009	0.225
\$ 50	134,575	.036	1.800
\$100	2,146,347	.583	58.300
\$250	1,369,318	.372	93.000
Total	3,682,332	1.000	\$153,325

The average deductible is about \$150.00.

3. BREAKDOWN OF RECOVERY FROM LIABILITY INSURER (1975 LOSSES)

Property Damage Coverage	Percent of Total Liability	Losses (\$million)	Claims	Claims x Deductible (\$million)	Losses Less Deductible (\$million)
Liability but not Collision					
Collision	25%	\$ 30	47,500	\$ 7	\$23
Liability and Collision	75	91	142,500	21	70
Total	100%	\$121	190,000	\$28	\$93

4. POTENTIAL RECOVERY BY DRIVER WITHOUT COLLISION COVERAGE AND AT FAULT

	675,000	Drivers presently without collision coverage
×	.087	Claims frequency (Collision)
	58,725	Potential claims
×	\$650	Average claim size (Collision)
	\$38,171,250	Total value of potential claims

BACKGROUND STUDY TWO

Government Ownership Of Automobile Insurance

TABLE OF CONTENTS

	Page
A. INTRODUCTION	391
B. BACKGROUND FOR GOVERNMENT OWNERSHIP OF AUTOMOBILE INSURANCE	392
1. Motivation	392
2. History of Government Insurers in Canada	393
3. The Motoring and Insurance Environment	397
C. PRODUCT DESCRIPTION	401
1. Basic Coverages	401
2. Premium Cost to the Consumer	407
3. Summary	408
D. OPERATIONS	409
1. Underwriting and Rating	409
2. Administration of Funds and Use of Profits	414
3. Marketing and Delivery System	415
4. Enforcement of Compulsory Insurance	420
5. Claims Handling and Settlement	421
6. Administration and Other Aspects of a Government Owned Corporation	427
7. Summary	430
E. FINANCIAL RESULTS AND COMMENTARY	431
1. Comparative Operating Results	431
2. Comparative Operating Costs	435
3. Comparative Efficiency	437
4. Summary	439
F. PUBLIC ACCEPTANCE	440
1. In the Government Ownership Provinces	440
2. In Other Jurisdictions	442
G. CONSEQUENCES OF GOVERNMENT OWNERSHIP	445
1. Advantages	445
2. Disadvantages	446
3. Further Considerations	449
	389

APPENDICES

Appendix A: Underwriting and Rating

Appendix B: Marketing and Delivery System

Appendix C: Descriptions of Claims Handling and Settlement

Appendix D: Adjustments to S.G.I.O. Results

BACKGROUND STUDY TWO

Government Ownership of Automobile Insurance

A. INTRODUCTION

“The Committee will seek to determine in detail the elements of public ownership of the automobile insurance business and how they vary from private ownership with a view to making recommendations on this issue.”¹

This study presents an outline of the experience with government ownership of automobile insurance in the three Provinces of Manitoba, Saskatchewan and British Columbia. The organization, products and operations of the Manitoba Public Insurance Corporation, the Saskatchewan Government Insurance Office, and the Insurance Corporation of British Columbia will be described with a view, first, to identifying possible advantages and disadvantages of government ownership, and, secondly, to identifying elements in their programmes that vary from the delivery of the insurance product by private insurance companies in Ontario.

The comments which follow have been summarized under the following headings:

B. Background for Government Ownership of Automobile Insurance

In this section of the study, the general motivation for government ownership is considered, followed by a brief review of the history of the government insurers in Canada. The motoring and insurance environment in the government ownership Provinces is also described and contrasted to the Ontario environment.

C. Product Comparison

This section provides a further review examining the nature of the insurance coverage provided by the government corporations and by private companies in Ontario. An illustrative comparison of premium cost differences concludes this section.

D. Operations

This section describes the revenue sources, programmes and operating methods of the provincial insurance corporations in an effort to demonstrate whether they experience any common problems or provide benefits that are presently not provided or not as well provided by the private insurance industry.

1. The Select Committee on Company Law, *The Insurance Industry—First Report on Automobile Insurance*, Province of Ontario Legislative Assembly, 1977, page 242.

E. Financial Comparisons and Commentary

Given the previous discussion of operations, this section examines the financial results of the provincial corporations to determine whether any of the savings attributed to government ownership are demonstrated in a financial comparison to industry results in Ontario.

F. Public Acceptance

The attitudes to government ownership of the government and public in Manitoba, Saskatchewan and British Columbia are surveyed in this section. In addition the question of government ownership in other jurisdictions is reviewed briefly.

G. Consequences of Government Ownership

This section summarizes the perceived advantages and disadvantages of government ownership.

B. BACKGROUND FOR GOVERNMENT OWNERSHIP OF AUTOMOBILE INSURANCE

1. Motivation

Motivation for government ownership of automobile insurance in Manitoba, Saskatchewan and British Columbia has been related to two factors: social principles and conditions in the insurance market. A brief review of the alleged motivating factors for government ownership follows.

It is argued that a major principle behind government ownership is the social necessity of compulsory minimum insurance. If private industry is allowed to market compulsory basic coverage, the motorist is forced to contribute to the profit of private companies. It may seem inappropriate for the motorist to be forced to contribute to the profit of a private company in a matter of social necessity. With the establishment of a compulsory market, it also may seem inappropriate that insurance should be provided at anything other than the lowest possible cost. A government automobile insurance enterprise is expected to produce economies of scale in administration and delivery costs that will permit operation at lower premium rates than other systems.

Furthermore, the principle of compulsory insurance requires that coverage be readily available to all motorists on an equitable basis. If conditions in the private market for insurance restrict the availability of coverage at reasonable cost to certain motorists, then it is argued that the principle of universal coverage may have to be met through government intervention.

Aside from the question of how best to market and administer compulsory insurance, a number of further socio-political aims may contribute to the motivation for government ownership. Firstly, government ownership is suggested as a means to ensure that the insurance carrier, because of its high

political profile and head office presence in the province, will be more sensitive to the needs and interests of the consumer.

Secondly, the claim is made that there may be the opportunity for the government insurer to utilize surplus funds, not for the interests of the shareholders of private insurance companies, but to a much greater extent in the interest of the public which contributes premiums to the insurance pool. This aim is said to be accomplished in several ways: by investing profits and reserves in the province to the fullest extent possible; by undertaking or funding programmes in the interests of the public, such as safety, rehabilitation or driver education programmes; or by returning excess monies to the premium payor to reduce his cost of insurance.

Thirdly, some argue for greater equity through government ownership in that the government insurer may be able, for social reasons, to justify the redistribution of the cost of insurance in such a way as to improve affordability, for example, by subsidizing groups of high risk drivers; or to spread the costs more equitably among all motorists, for example, by charging all drivers and not just owners. However, with all the above socio-political motives, there appears to be a danger that what may be socially desirable for the many, may not be desirable for given groups or sub-groups within the population, or may not be acceptable because of financial constraints.

The changeover to government ownership of automobile insurance in Saskatchewan, Manitoba and British Columbia was largely motivated by the philosophical principle that compulsory basic automobile insurance should be provided in a non-profit manner by a corporation whose interests rest with the motoring public in the Province. In Saskatchewan, limited availability of insurance through the voluntary market contributed perhaps more heavily to the decision towards government involvement than in Manitoba and British Columbia, where market conditions may have been termed unsatisfactory but were not drastically so. A brief history of the introduction of government ownership of automobile insurance in these three Provinces follows.

2. History of Government Ownership in Canada

Saskatchewan Government Insurance Office

The Saskatchewan government began its involvement in public administration of insurance in 1944 when an Act of the Legislature established a public corporation, the Saskatchewan Government Insurance Office (S.G.I.O.), to engage in the business of general insurance. Government involvement was called for because the voluntary general insurance market was not serving rural communities adequately. S.G.I.O. was created to service the market in competition with private insurers.

In 1945, a study of compensation in automobile accident cases found that compensation was seriously inadequate; that only 12% of motorists at that time were insured under third-party liability coverage; and that generally automobile insurance was neither available nor affordable. Subsequently in 1946, the Automobile Accident Insurance Act (A.A.I.A.) was passed, involving S.G.I.O. in the administration of a compulsory programme of basic minimum no-fault protection for the automobile accident victim. Over the intervening 32 years this programme has been progressively modified to include a higher level of Accident Benefits coverage; mandatory minimum liability coverage of \$35,000; and compulsory first-party coverage for vehicle damage, with a standard deductible of \$200 on passenger vehicles.

The A.A.I.A. programme provides a compulsory "basic coverage package" for the Saskatchewan motorist. A voluntary second-tier, or "extension coverage package", is available from both S.G.I.O. and from private insurers so that liability limits can be increased and deductibles can be reduced to meet the needs of the individual. In practice it is estimated that S.G.I.O. accounts for about 75% of the policies written for extension coverage and its share of this market is growing.

Manitoba Public Insurance Corporation

The Manitoba Public Insurance Corporation (M.P.I.C.), a Crown Corporation established by Manitoba's Automobile Insurance Act of 1970, commenced operations on November 1, 1971 to administer, as the exclusive supplier, a comprehensive automobile insurance plan, known as Autopac.

During the period prior to the introduction of Autopac, returns of private insurers had indicated the following conditions in the market:

- at least 3% of vehicle owners were uninsured for third-party liability coverage;
- 55% did not have the protection of Accident Benefits coverage;
- 26% did not insure their vehicles against collision damage;
- 6% did not have fire and theft insurance; and
- 71% of vehicle owners did not carry medical payments coverages.

The Government of Manitoba decided in 1970 that there was a need to make basic coverage compulsory and in 1971 that a compulsory market could best be served by government administration of automobile insurance funds.

The Manitoba automobile insurance programme is similar to that of Saskatchewan in that it provides a basic compulsory package of Accident Benefits coverage; third-party liability coverage with a minimum limit of \$50,000; and all perils vehicle coverage subject to a \$200 deductible on passenger vehicles.

Additional coverage is available on a voluntary or optional basis from Autopac or from private insurers. It is estimated that because of the convenience of "one stop" shopping and claims settlement for both compulsory and optional coverage, M.P.I.C. policies account for 85% of the extension coverage market.

Manitoba's Automobile Insurance Act was revised in 1974 and re-named The Manitoba Public Insurance Corporation Act. This statute now provides the legal basis for administration of the automobile insurance programme and it also provides the Corporation with authority to operate in other fields of insurance. On July 2, 1975, the Corporation officially began marketing various classes of general insurance through its agency force in Manitoba.

Insurance Corporation of British Columbia

The Insurance Corporation of British Columbia (I.C.B.C.) was created in April 1973 as a Provincial Crown Corporation to engage in and carry on the business of insurance in all classes. The Corporation's primary function is to provide and administer Autoplan, a non-profit automobile insurance programme established under the Automobile Insurance Act and brought into operation on March 1, 1974.

Prior to the creation of I.C.B.C., the Province enacted legislation in 1970 which made it mandatory that all motorists carry third-party liability insurance and, later in the same year, that motorists be required to carry Accident Benefits coverage. This legislation, following recommendations of the 1968 British Columbia Royal Commission on Automobile Insurance, greatly reduced the number of uninsured vehicles in the Province, but did not eliminate them. Five percent of motorists remained uninsured for third-party liability coverage.

Prior to Autoplan, a number of further problems were cited in the British Columbia market:

- Efforts to cope with a large residual market were divided between the operations of two different high risk plans, the "Facility", and the "B.C. Insurance Exchange";
- "Creaming" of the market was practised by insurers, who enjoyed the privileges of being selective in the risks they chose. This was considered to be an undesirable practice, resulting in alleged gaps of availability;
- Increasing claims costs and processing delays were said to be creating dissatisfaction with the system as operated by the private industry;
- Mid-term and arbitrary cancellation by insurers was said to be widespread;
- A poor relationship existed between insurers and automobile owners, giving rise to frequently heard criticism that the insurers were controlled from a distance and had no interest for local needs;
- The industry and the adversary system were accused of being inefficient. Only 62.5% of the premium dollar was said to be returned by the industry to the consumer.

The Royal Commission of 1968 had made recommendations to deal with these apparent problems but had cautioned that, if the industry failed to implement sufficient improvements, then the government of the Province of British Columbia should take over, as the sole supplier, the role of selling automobile insurance in that Province.

The government ownership alternative was adopted only a few years later by the New Democratic Party government of the day who intended that the operation of Autoplan by a government corporation would improve the delivery of the automobile insurance product. The legislation passed in 1973 provided that I.C.B.C. would have exclusive responsibility, with only a few specific exceptions, for providing all automobile insurance required by B.C. motorists. Private insurers subsequently withdrew from the automobile insurance market.

After the 1976 change of government, collision and comprehensive coverage was taken out of the compulsory programme and was made available on an optional basis. At the same time, the market for voluntary extension coverage, including all coverages involving vehicle damage only, was opened up to participation by private insurers. Private industry however has been reluctant to return, except in a very selective way, and as a result it is estimated that I.C.B.C. writes about 98% of extension third-party liability and collision and comprehensive coverage.

Autoplan today provides both the basic compulsory coverage, consisting of third-party liability coverage of at least \$75,000 together with Accident Benefits coverage; and also the optional coverages, extending liability

limits and providing all normal forms of property damage insurance with flexible deductible amounts to meet the needs of the individual insured.

Current Market Position

The participation of the government insurers in the automobile and general insurance business in the respective Provinces is shown in Table 1 below.

TABLE 1
THE AUTOMOBILE AND GENERAL INSURANCE MARKET

1976 Direct Premiums Written (\$ million)	Manitoba		Saskatchewan		British Columbia	
	M.P.I.C.	Private Market	S.G.I.O.	Private Market	I.C.B.C.	Private Market
Automobile Insurance						
Compulsory	\$83.5		\$77.6		\$201.0	
Extension	13.0	\$ 2.3	14.3	\$ 4.5	150.0	\$ 2.4
General Insurance	7.3	109.6	38.1	69.6	25.1	363.8
Market Share						
Automobile Insurance						
Compulsory	100%	—	100%	—	100%	—
Extension	85%	15%	76%	24%	98%	2%
General Insurance	6%	94%	35%	65%	6%	94%

Source: Federal Superintendent of Insurance, *Annual Report*, Business of 1976, and M.P.I.C., S.G.I.O., I.C.B.C. estimates.

The automobile insurance business of I.C.B.C. is roughly four times larger than the corresponding business of S.G.I.O. and M.P.I.C. Furthermore the extension coverage market, which is open to private insurers in all three Provinces, is substantially greater in British Columbia. Contributing to this difference is the inclusion of collision and comprehensive coverage in the extension market rather than in the compulsory insurance component as in Manitoba and Saskatchewan.

All three provincial corporations account for 100% of the compulsory automobile insurance market in their respective Provinces and for a major share of the extension coverage market. S.G.I.O. is the largest general insurer of the three provincial corporations and it holds a significant share of the Saskatchewan general insurance market.

3. The Motoring and Insurance Environment

To provide a better perspective in which to consider the question of government ownership, the motoring and insurance environment in the government ownership Provinces and its relevance to Ontario is briefly outlined below.

Vehicles and Accidents

Table 2 provides a brief summary of statistics related to motoring and accident experience in the three government ownership Provinces in comparison to Ontario. Total motor vehicle registrations in the three Western

TABLE 2
THE MOTORING ENVIRONMENT

	Ontario	Manitoba	Saskatchewan	British Columbia
<i>Roads and Vehicles</i>				
Drivers Licences (1975)*	4.2	0.5	0.6	1.6
Total Motor-Vehicle Registrations* (1975)	4.1	0.5	0.7	1.6
Passenger Vehicle Registrations* (1975)	3.4	0.4	0.3	1.2
Miles of Paved Roads (1973)	38,200	6,800	11,300	16,500
Motor-Vehicles per Mile of Roads and Streets (1973)	37.3	9.2	4.2	33.4
<i>Accidents (1975)</i>				
Number of Accidents	213,700	36,300	27,400	85,500
Number of Accidents per Hundred Vehicles	5.2	7.3	3.9	5.3
Accidents per Million Vehicle Miles:				
Property Damage	2.9	5.9	3.7	5.3
Injuries	2.5	2.3	2.4	2.3
Urban Accidents as Percent of Total	53%	79%	57%	70%
<i>Traffic Laws</i>				
Mandatory Seatbelts	Jan./76	No	Oct./76	Oct./77
Speed Laws	100 km/hr.	100 km/hr.	100 km/hr.	100 km/hr.

* millions

Source: Statistics Canada

M.P.I.C., S.G.I.O., I.C.B.C.

Canada Safety Council

Provinces combined account for only about 70% of the vehicle population in Ontario. Similarly, the number of accidents in all three Provinces combined amounts to only 70% of the number in Ontario. The insurance market is correspondingly much smaller.

While Manitoba and Saskatchewan show a low density of vehicles per mile of road and street, British Columbia is very similar to Ontario in that it has a high density of motor vehicles on its roads.

Despite a smaller vehicle population, both Manitoba and British Columbia, particularly in the Lower Mainland region, share in many of the problems of high accident frequency encountered in Ontario. Both Manitoba and British Columbia stand out in their high proportion of accidents on urban roads as opposed to rural roads, and in a much higher rate of property damage accidents per million vehicle miles travelled. Manitoba in particular appears to be accident-prone.

In general, the motoring environment in British Columbia is the most similar to that of Ontario, mainly with respect to motor vehicles per mile of road and street. The significantly smaller vehicle populations in Manitoba and Saskatchewan provide an obviously different context for the implementation of government ownership than would be the case in Ontario.

TABLE 3
THE AUTOMOBILE INSURANCE ENVIRONMENT

	Ontario	Manitoba	Saskatchewan	Columbia
<i>The Automobile Insurance Market</i>				
Direct Premiums Written (\$ million), 1976	\$983.2	\$96.5	\$91.9	\$351.8
Size of Ontario Market Relative to Other Provinces		10 times larger	11 times larger	2-3 times larger
<i>Present Automobile Insurance Coverage</i>				
Residual Market	6.7%	none	none	none
Accident Benefits Coverage	mandatory 1972	mandatory 1970	mandatory 1946	mandatory 1970
Uninsured Motorist: At Present	7-12%	Under 1%	Under 1%	Under 1%
Prior to Government Ownership	—	3% (1970)	88% (1946)	5% (1971)
Motorists With No Collision Coverage	25-27%	None	None	About 20-25%
<i>Litigation</i>				
Percent of Total Auto Claims Resulting in Start of Court Action	2-3%	0.4%	Well Under 1%	0.4%
Approximate Number of Lawsuits Filed, 1976	15,000	725	Under 1,000	2,000
Lawsuits per 1,000 Registered Vehicles	3.6	1.4	1.4	1.2

Sources: S.G.I.O., M.P.I.C. and I.C.B.C.
Insurance Bureau of Canada
Ministry of the Attorney General, Ontario
Report of the Federal Superintendent of Insurance,
Business of 1976

The Size of the Automobile Insurance Markets

As is evident from Table 3, the automobile insurance market in Ontario cannot be compared in size to the three government ownership Provinces: it is ten to eleven times larger than the government administered markets in each of Manitoba and Saskatchewan, and two to three times larger than the market held by I.C.B.C. in British Columbia. In Ontario bodily injury coverage alone (10 percent of claims, 40 percent of total costs) is roughly the size of the total market in British Columbia.

Insurance Coverage

The government ownership Provinces, as shown in Table 3, have resolved the problems of the uninsured motorist and have eliminated the need for a mechanism to handle the residual market. All three Provinces expressed dissatisfaction with the way the private voluntary market was handling the high risk driver prior to government ownership. However, in the case of Saskatchewan, its experience prior to government ownership is not

relevant to the situation in Ontario today, because that experience occurred over three decades ago under vastly different conditions. It is also difficult to ascertain from the past experiences of the other two government ownership Provinces whether their problems of insurance availability and coverage prior to government ownership were any more severe than they are in Ontario today.

With the exception of Saskatchewan in the 1940's, availability of some form of no-fault coverage or Accident Benefits coverage was not an issue leading to government ownership. Accident Benefits coverage was made mandatory in both Manitoba and British Columbia in 1970 and was not significantly revised by the government insurer.

In structuring a package of coverage under government ownership, the question arises whether collision coverage should be made compulsory and therefore part of the basic coverage package, or voluntary and thus a part of the extension coverage options. At the present time, Manitoba and Saskatchewan have provisions for compulsory collision coverage, whereas in Ontario and British Columbia approximately one-quarter of drivers carry no collision cover. As a comparison, roughly 26% of drivers in Manitoba had no collision coverage prior to government ownership. Compulsory collision coverage has skewed the distribution of the claim dollar heavily towards property damage, particularly in Saskatchewan. A more detailed product comparison is provided in Section C.

Litigation

The government ownership Provinces currently have a lower frequency of litigation in comparison with Ontario. Furthermore, given the larger size of the insurance market in Ontario, even the apparently low percentage of claims that go to court result in a substantially greater court load than in the other Provinces. The number of court actions per year in Ontario is roughly seven times higher than in British Columbia, while the population and the incidence of accidents is only about three times higher.

C. PRODUCT DESCRIPTION

This section provides a review of the nature of the insurance coverage provided by the provincial corporations and by the private sector in Ontario. An illustrative comparison of premium costs in the four Provinces of Ontario, Manitoba, Saskatchewan and British Columbia is also provided.

1. Basic Coverages

In all four Provinces, the basic coverages available to the automobile owner are the same: third-party liability coverage, Accident Benefits coverage, and collision and comprehensive coverage. Basic coverages as well as specific benefits in the automobile insurance plans of Ontario, Manitoba, Saskatchewan and British Columbia are outlined in Table 4.

Coverages That Are Compulsory

Third-party liability coverage and Accident Benefits coverage are compulsory in all three government ownership Provinces. In comparison, third-party liability coverage is still voluntary in Ontario although an announcement has been made by the government that it is to become compulsory. At the present time, Accident Benefits coverage in Ontario is only compulsory when third-party liability coverage is purchased.

Collision coverage, with a standard deductible of \$200, in the case of passenger vehicles, is compulsory in Manitoba and Saskatchewan. In British Columbia and Ontario, collision coverage is optional.

Accident Benefits Coverage

Benefits paid without regard to fault under Accident Benefits are at the present time similar in all four Provinces, but include a number of specific variations within categories of loss. However, in Ontario the government has announced an enrichment of Accident Benefits coverage effective on

TABLE 2
INSURANCE COVERAGE: PRIVATE AND GOVERNMENT AUTOMOBILE
INSURANCE IN MARYLAND, PENNSYLVANIA AND DISTRICT OF COLUMBIA

	NEW YORK	MARYLAND	PENNSYLVANIA	DISTRICT OF COLUMBIA
TOTAL AUTOMOBILE	A. Liability Coverage Compulsory Voluntary	Compulsory only under liability coverage No	Yes No	Yes No
	B. Liability Coverage Compulsory minimum Voluntary	No \$100,000 Minimum	\$100,000 limit deductible	\$100,000 limit deductible
	C. Liability Coverage Voluntary	No With choice of deductible	Yes, \$200 deductible Lower deductible	Yes, \$200 deductible Lower deductible
VOLUNTARY	Compulsory coverage Voluntary Coverage	- Private Insurers	MDIC (public corporation) MDIC and private insurance	MDIC (public corporation) MDIC and private insurance
	Basic Accident Benefits (Deductible)	Chiricments July 1, 1979		
SALE AND SERVICE BENEFITS	1. Death benefits: a) Funeral expenses b) Death of household head c) Death of spouse d) maintenance for dependents e) limit	\$500 \$1,000 \$2,000 \$10,000 each no limit	\$500 \$1,000 \$2,000 \$10,000 each \$10,000	\$750 \$1,000 \$2,000 \$10,000 each \$10,000
	2. Medical Expenses	\$5,000 (\$25,000)	\$2,000	\$5,000
	3. Compensation (Deductible) None	none	\$1,000 each	\$1,000 each
PREMIUM	a) Basic loss (amount) b) Total liability c) Partial disability d) Injury to household	\$10/wk./100 weeks (\$100/wk) First day - \$10/wk./17 weeks (\$100/wk.)	\$75/wk./lifetime 7 days \$275/wk./life saving \$20/wk./12 weeks	\$75/wk./lifetime 5 weeks \$275/wk./life saving \$20/wk./12 weeks
	1. Vehicle Premium • age and sex • marital status • vehicle use • territory • number of vehicles	1. Vehicle Premium Fee • make, model, year • territory, body • vehicle use • vehicle age • territory	1. Vehicle Premium Fee • make, year and type of vehicle • territory, body • vehicle use • vehicle age • territory	1. Vehicle Premium Fee • age and sex • marital status • vehicle use • territory • number of vehicles
	2. Vehicle Premium Fee • age and sex • driver record	2. Vehicle Premium Fee • age and sex and driver record	2. Vehicle Premium Fee • age and sex and driver record	2. Vehicle Premium Fee • age and sex and driver record
	3. License Tax = 1% of value	3. License Tax = 1% of value	3. License Tax = 1% of value	3. License Tax = 1% of value

July 1, 1978 which will increase benefit amounts payable to all injured persons.

The maximum amount payable for medical expenses currently varies from \$2,000 in Manitoba to \$4,000 and \$5,000 in Saskatchewan and Ontario. In contrast, British Columbia provides for a substantially higher limit amounting to at least \$75,000, and increasing to \$100,000 if liability coverage is bought in excess of that amount. The Ontario limit will be increased to \$25,000 per person in July 1978.

Death benefits in Saskatchewan and British Columbia are at present richer than in Ontario and in Manitoba. Saskatchewan provides a higher principal death benefit of \$7,500, while British Columbia, in addition to the fixed-sum payment of \$5,000, also includes wage-related benefits over a two year period. As Table 4 shows, Ontario is revising its death benefits to amounts that will exceed payments in the government ownership Provinces, except to the extent of weekly indemnity payments in British Columbia.

Wage loss indemnity in the government ownership Provinces has not been significantly different from the amounts payable in Ontario, although Manitoba and Saskatchewan pay benefits on a lifetime basis. However, beginning July 1978, Ontario benefits for loss of income will increase to a limit of \$140 per week. In addition, benefits in Ontario are payable from the first day of injury compared to the seventh day after the accident in each of the other Provinces. Both Manitoba and Saskatchewan provide payments for partial disability and dismemberment benefits which are not available in Ontario or British Columbia.

In general, the automobile accident victim in Manitoba and Saskatchewan at present does not receive any more in Accident Benefits payments than his Ontario counterpart. British Columbia currently provides a somewhat richer package, with higher no-fault benefits in the categories of medical and death benefits. With enrichment of Accident Benefits coverage in July 1978, Ontario will increase no-fault protection to a level higher in general than that provided in the government ownership Provinces.

The standard Ontario automobile insurance policy lists a number of circumstances which result in breach of condition and denial of Accident Benefits payments, and the Automobile Insurance Acts in the three government ownership Provinces have similar provisions. For example in British Columbia, persons attempting to escape arrest and persons receiving U.I.C. benefits are excluded from any right to receive Accident Benefits payments. Ontario policies do not contain these exclusions.

On the other hand, in British Columbia, the person convicted of impaired or drunken driving is not excluded from Accident Benefits coverage although he is excluded from recovery under collision coverage. In Manitoba, death payments and funeral benefits are paid in cases of impaired driv-

ing, but wage benefits are not. Accident Benefits are denied to impaired drivers in both Saskatchewan and Ontario. In Saskatchewan a suicide or attempted suicide does not result in loss of eligibility, whereas suicide is a disqualifying factor in all three other Provinces.

In the three government ownership Provinces, misrepresentation regarding the insurance certificate, or an expired licence or registration excludes a driver from coverage. This is not the case in Ontario, where the insurance transaction is separate from the licencing system.

In general, the government ownership Provinces set up exclusions from Accident Benefits coverage in several areas not defined in the standard Ontario policy. The motorist buying basic coverage is frequently unaware (as in Ontario) that he is not covered in certain circumstances under compulsory insurance policies.

Third-Party Liability Coverage

The Ontario requirement of \$100,000 minimum third-party liability coverage is the highest in North America. British Columbia has recently raised its limits to the \$75,000 level, approaching those of Ontario, while in Saskatchewan and Manitoba the minimum limits are \$35,000 and \$50,000 respectively.

Every motorist in the three government ownership Provinces must carry third-party liability coverage. In Ontario, it is estimated that about ten percent of drivers choose to remain uninsured; about three percent contribute to the Motor Vehicle Accident Claims Fund instead of obtaining insurance, while the remaining six percent or so neither carry insurance nor contribute to the Fund.

Many motorists in the government ownership Provinces as well as in Ontario carry third-party liability coverage well in excess of the mandatory limits. For example, in Saskatchewan, all drivers purchase the \$35,000 compulsory coverage, while a major segment is said to purchase an additional \$200,000 extension policy. In British Columbia, it costs the driver only \$4 extra to raise his coverage to the Ontario limit of \$100,000. I.B.C. statistics indicate that in Ontario sixty percent of private passenger vehicles are insured for third-party liability coverage in excess of \$100,000.

Third-party liability coverage in Saskatchewan does not include Passenger Hazard coverage, which must be purchased separately in an extension policy. It is claimed that most Saskatchewan motorists are unaware of this gap in their basic liability insurance policy.

The three government ownership Provinces provide for uninsured motor vehicle coverage in the compulsory insurance package for all accidents that occur in the Province. In addition, pedestrians and out-of-province vehicles and their occupants are compensated by the government cor-

poration itself in cases of accident with an unidentified or uninsured driver, so that there is no need for a separate unsatisfied judgement fund. Uninsured motor vehicle coverage for out-of-province accidents must be purchased separately or recovery must be made under the unsatisfied judgement fund of the relevant jurisdiction. In Ontario, the Motor Vehicle Accident Claims Fund provides for recovery up to \$100,000. For recovery in other jurisdictions separate uninsured motorist coverage can be purchased or recovery can be referred to the relevant unsatisfied judgement fund.

Own-Vehicle Damage Coverage

The consumer in all four Provinces under study is able to purchase a comparable level of coverage for damage to his own vehicle. The only difference to be considered is who he buys it from, a private or government insurer, and whether or not he is compelled to buy.

In Manitoba and Saskatchewan, purchase of own-vehicle coverage is compulsory. Basic coverage with a \$200 deductible on passenger cars must be bought from the government corporation. In Saskatchewan, compulsory own-vehicle coverage provides "comprehensive" coverage; in Manitoba, this compulsory coverage also includes "all perils" protection. In Manitoba, when loss or damage is caused by fire, lightning or theft, the compulsory coverage pays the entire amount of the loss, less depreciation, whereas in Saskatchewan, the compulsory coverage does not pay the deductible amount of \$200.

Additional own-vehicle coverage or a lower deductible coverage can be purchased either from private insurers or from the government corporation. Compulsory coverage in Saskatchewan has been criticized because of the unsatisfactory way in which it covers certain situations: for example, in hit and run collisions full coverage is provided only for damage exceeding the \$200 deductible, even if the claimant had no fault in the accident. Optional collision coverage in British Columbia has the same provision.

In Ontario and British Columbia, own-vehicle coverage is optional and can be purchased in both Provinces from private insurance companies, or alternatively in British Columbia from the provincial corporation. I.C.B.C. sells all normal forms of own-vehicle coverage and is in practical terms almost the sole supplier since it writes about 98% of the policies written in the Province.

Product Awareness

Motorists in the government ownership Provinces do not receive a copy of the automobile insurance policy. Instead, each of the government insurers prints a guide to insurance coverage that is available to consumers on demand. Yet it is generally acknowledged that the consumer is very often unaware of the provisions in his basic insurance policy and may not be fully

TABLE 5
RECENT PREMIUM COMPARISON BY CITY

	COVERAGE:	LIABILITY		\$200,000 INCLUSIVE		\$ 100 DEDUCTIBLE		\$ 50 DEDUCTIBLE			
		COLLISION									
		COMPREHENSIVE									
		ACCIDENT FREE*				NOT ACCIDENT FREE					
		Pleasure Not Driven to Work \$	Pleasure Driven to Work \$	Under Age 25, Female \$	Under Age 25, Male \$	Pleasure Not Driven to Work \$	Pleasure Driven to Work \$	Business \$	Under Age 25, Female \$	Under Age 25, Male \$	
1976 Ford Granada											
Toronto		321	371	444	475	784	537	624	754	811	1,360
Ottawa		305	350	415	451	738	500	580	697	760	1,272
Vancouver		270	333	452	402	650**	360	444	602	536	1,156
Winnipeg		192	234	304	234	234	192	234	304	234	234
Regina		224	224	248	260	260	238	238	261	273	273
1968 Chevrolet											
Station Wagon											
Toronto		256	298	358	369	607	433	506	612	633	1,056
Ottawa		234	270	321	336	549	387	452	544	571	950
Vancouver		184	227	284	267	440**	245	303	402	356	782
Winnipeg		135	169	214	169	169	135	169	214	169	169
Regina		124	124	148	160	160	138	138	161	173	173

* The premiums shown for B.C. are based on the motorist having a two-year claim-free period from October 1, 1975 to September 30, 1977. Premiums shown for other provinces are for drivers who had 3 year accident-free records.

** The under 25 single male premium reflects the 25% Safe Driving Incentive Grant paid by cheque for drivers free of blameworthy claims and with less than 6 penalty points on their current record.

Note: Toronto and Ottawa rates are suggested by the Insurers' Advisory Organization, July 1977.

Source: Insurance Corporation of British Columbia, March 1, 1978.

aware of the need for extended coverage. It is therefore clear that government ownership does not solve the problem of consumer ignorance of the nature of the insurance product. It may even instill in the consumer a false complacency about the adequacy of his basic coverage.

2. Premium Cost to the Consumer

The motorist in the government ownership Provinces is paying for automobile insurance in a number of ways other than direct premiums. As there is concern that government grants and other methods of deriving income may serve to mask the true costs of operating government insurance organizations and may distort premium comparisons, this matter is examined in some detail in Sections D and E of this study.

However, the matter of a premium comparison is of general interest in any discussion of government ownership. Accordingly, Table 5 is provided in this study to illustrate some of the general characteristics of premium rates in the three government ownership Provinces and in Ontario. The premium rates shown in this table for Toronto and Ottawa are rates suggested as a benchmark by the Insurers' Advisory Organization (I.A.O.) for use by its members in developing their own rates. Recent experience in Ontario indicates that most companies are writing policies at rates below those suggested by I.A.O. Therefore, Table 5 should not be used as the sole or conclusive measure of premium rate differences in the four Provinces. Given these qualifications, the following discussion simply presents several observations on the data provided in Table 5.

Premiums shown in Table 5 for Vancouver, Winnipeg and Regina are well below those for comparable coverages in Toronto and Ottawa. Differences in geography and in the vehicle population, for example in the cities of Winnipeg and Toronto, likely explain much of the variance. Other sources of income available to the government corporations but not indicated in Table 5 also contribute to lower premium rate levels, particularly in Manitoba and Saskatchewan. I.C.B.C. premium levels are least affected by other sources of income as data later in this study show that premiums make up approximately 98% of total revenues collected from consumers.

Vancouver rates come closest to matching the level and pattern of rates in Toronto and Ottawa. Noteworthy, however, is the relatively high rate that is charged in Vancouver for the accident-free driver who uses his car for business purposes. This rate is significantly higher than rates in Winnipeg and Regina, and may even be higher than the rates in Toronto and Ottawa for the accident-free driver.

Manitoba and Saskatchewan rates are relatively "flat" across all categories of driver. Manitoba in particular does not take into account accident records in setting premium rates for either compulsory or extension coverage. Ontario rates and those in Vancouver increase substantially when

"higher risk" categories of driver are considered, such as the under 25, male driver with an accident record. Manitoba and Saskatchewan impose less of a premium penalty on the high risk driver although, in the case of a poor driving or accident record, surcharges are applied as a drivers' licence fee. Instead, the business use driver in these Provinces appears to bear a relatively greater premium burden. Although not apparent from this table, lack of emphasis on territorial rating in Manitoba and Saskatchewan, with only one territory in Saskatchewan and four in Manitoba creates a situation wherein the rural driver tends to subsidize the possibly more accident-prone urban driver. This subsidization can be a source of dissatisfaction.

Vancouver is perhaps most comparable to the rating situation in Toronto and Ottawa in terms of a large vehicle population and a rating structure composed of numerous classifications. On average, premium rates shown in Table 5 for Vancouver are lower than rates suggested by I.A.O. for Toronto and Ottawa.

A conclusive comparison of the average dollar cost of the automobile insurance product is not possible without obtaining premium quotations for numerous rate categories from a cross-section of leading Ontario insurers and accounting for all sources of income collected from consumers in the government ownership Provinces. Even with this information, differences in geography, climate and vehicle population may distort premium comparisons. Therefore, such a comparison is not attempted in this section; instead Section E provides what is considered to be a more meaningful measure of "cost" as related to the efficiency of the government ownership and private industry systems.

3. Summary

In summary, it is evident that the vehicle owner or accident victim is not necessarily any better protected under the terms of his compulsory coverage in the government ownership Provinces, than in Ontario under the terms of the standard automobile policy. The traditional coverages, third-party liability coverage, Accident Benefits coverage and own-vehicle coverage, are substantially the same in the government ownership Provinces as those available in Ontario. However, Ontario's minimum liability limit and its soon to be enriched Accident Benefits coverage are more generous than the protection provided in the Western Provinces.

Differences which do exist in the insurance product can be made minimal. The consumer in all four Provinces under study is able to purchase a comparable level of coverage by selecting appropriate options in conjunction with compulsory coverage. The consumer's ignorance of the provisions of his insurance policy may prevent him from purchasing a sufficient level of coverage both in Ontario and in the three government ownership Provinces.

The premium costs of similar levels of coverage in each Province cannot be easily compared in a fashion that reflects relative costs in similar insurance environments. More meaningful than a premium cost comparison might be the measurement of efficiency in each system as discussed later in this study.

D. OPERATIONS

This section describes the revenue sources, programmes and operating methods of the government insurance corporations in an effort to demonstrate whether they experience any common problems or whether they provide any benefits to the motorists and residents in those Provinces that are not provided or not as well provided in Ontario by the private insurance industry. The following review of operations is organized under the following headings:

- Underwriting and Rating
- Administration of Funds and Use of Profits
- Marketing and Delivery System
- Enforcement of Compulsory Insurance
- Claims Handling and Settlement
- Administration and Other Aspects of a Government Owned Corporation

1. Underwriting and Rating

Risk Selection

Underwriting in a private enterprise market for automobile insurance often results in a problem: the possible inability of some higher risk drivers to obtain coverage as a result of the risk selection policies and practices of competitive insurers. Under existing legislation, private insurers are able to determine selectively the risks they wish to accept. They may decide to market only to preferred rate classes or they may apply a judgement rating that effectively denies coverage to "bad" drivers. Often these "bad" drivers are identified on the basis of a subjective evaluation of risk.

The industry has responded to this problem in a variety of ways, such as the use of assigned risk plans, facilities and joint underwriting agreements. The establishment of an effective residual market mechanism is required in order to permit the industry to practice its risk selection policies without restricting the availability of coverage.

In contrast, a government insurer must accept all risks. As a result there is no residual market and no need for a mechanism to handle residual business.

Rating

The government automobile insurance corporations share with private industry the problems of structuring a fully acceptable and equitable rate classification system. The particular underwriting philosophy of each government insurer determines how broadly or narrowly rate classes are defined. Nevertheless, government ownership provides the consumer with a uniform classification system, reducing the confusion that is often cited under the private sector, wherein each insurer may have its own method of applying rating classification factors. The government insurers in Western Canada ensure that all insureds are assessed premium rates on a basis of uniform criteria. This practice complies with the Committee's recommendations for Ontario:

"It is the Committee's intention that the present underwriting practice of taking various subjective factors into consideration in deciding whether to write a policy should be abolished. An applicant should then be judged on the basis only of the authorized criteria and he will be entitled to have his premium calculated accordingly . . ."¹

A detailed outline of premium sources and the rate classification system in the three government ownership Provinces is provided in Appendix A as background to the discussion which follows.

In Manitoba and Saskatchewan, the rating classification system is based on a limited number of simple facts. Rate categories determined by "risk" classification of the vehicle owner on the basis of personal characteristics, such as age, sex, or marital status, are not utilized by underwriters of compulsory coverage in Saskatchewan nor by underwriters of either compulsory or extension coverage in Manitoba. While S.G.I.O. has decided to implement a relatively flat or uniform system of rating for its compulsory coverage, it continues to use more "traditional" rating factors in setting premiums for its extension coverage.

As a one-company provider of basic third-party liability insurance coverage, the government insurance corporations in Manitoba, Saskatchewan and British Columbia are in the unique position of being able to incorporate in their overall rating system, methods of matching a number of sources of "premium" income with various rating factors. Both Manitoba and Saskatchewan have applied this technique in similar ways by relating:

- The use of the vehicle to gasoline tax and a drivers' licence fee.
- The value of the vehicle to a certificate of insurance premium.
- The driver's record to demerit point surcharges as part of the drivers' licence fee.

1. Select Committee on Company Law, *First Report on Automobile Insurance*, page 124.

Both Provinces have disregarded certain more traditional "risk" factors, for example, personal characteristics such as age and sex and other factors such as driving experience, in determining rates for basic coverage.

In Manitoba there are four rating territories while Saskatchewan has eliminated territorial ratings. While there is some resentment among rural drivers in Saskatchewan that they are subsidizing urban drivers, in general, both Manitoba and Saskatchewan vehicle owners are relatively complacent about their automobile insurance system and are not voicing any strong grievances related to the broad classification structure for rating.

On the other hand, public concern over good drivers bearing some of the premium burden for poor drivers has been apparent in British Columbia. The underwriting department of the Insurance Corporation of British Columbia initially simplified the number of rate categories applicable to both compulsory and extension coverage. However, I.C.B.C. returned to the use of a comprehensive set of rate classes along more traditional lines and it is now evaluating additional rate classes, primarily in the under 25 age group of drivers. As a result, the I.C.B.C. rating system is very similar to that of private industry and probably absorbs a higher budget for the underwriting function than in the other two government ownership Provinces.

It is interesting to note that the British Columbia government, when I.C.B.C. was being organized, made a commitment to the drivers in the Province that their premium rates would not be any higher under government ownership than under the private industry system. But simplification of the rate classification system by I.C.B.C. produced an increase in rates for drivers in certain categories of driver, who were then allowed to apply for refunds.

The young drivers were particularly affected by changing rate levels. I.C.B.C. initially reduced rates for many young drivers, with a resulting higher premium burden on the older motorist. When I.C.B.C. returned to a more traditional rate classification system with greater emphasis on age, sex and marital status, rates for young drivers "sky-rocketed". The inflationary environment at the time and the overgenerous attitude of I.C.B.C. settlements contributed further to a significant rise in costs that was reflected in higher premiums across the board and particularly for the young driver.

The British Columbia example illustrates the possibility under government ownership of political intervention in the ratemaking process which may not be consistent with actuarial principles. Nevertheless, such intervention in the government ownership Provinces may be deemed to be socially desirable in order to achieve social goals such as making compulsory insurance more affordable to drivers in high risk categories.

Income Sources

The underwriting group in the government automobile insurance corporation concentrates on a yearly determination of premium levels by evaluating loss experience in the relevant rate classes together with other sources of income and with the payout respecting claims and expenses. When these factors are determined, a basic premium is set at the level which would provide a break even operation.

It is important to note that in setting their premiums, the government underwriters may be able to take into account income from a variety of sources not available to the private insurance company. The government corporation may be able to obtain access to fees charged to the motorist at the time of motor vehicle registration or driver licence renewal, or it may be able to draw upon tax revenue such as the gasoline tax.

The table below outlines the sources and relative distribution of income collected by the automobile insurance funds in the government ownership Provinces.

TABLE 6
DISTRIBUTION OF INCOME COLLECTED UNDER
THE AUTOMOBILE INSURANCE FUNDS, 1976

	Saskatchewan		Manitoba		British Columbia	
	\$Million	Percent	\$Million	Percent	\$Million	Percent
Certificate of Insurance Premium	\$57.5*	77%	\$72.3**	77%	\$347.3**	90%
Drivers' Licence Fees	—	8	10.6	11	7.5	2
Gasoline Tax	11.0	15	6.5	7	—	—
Investment Income	6.1	8	4.5	5	30.2	8
Total Revenues	\$74.6	100%	\$93.9	100%	\$385.0	100%

* Basic Coverage only, includes drivers' licence fees.

** Basic and Extension Coverage.

Source: Financial statements of S.G.I.O., M.P.I.C. and I.C.B.C.

All three Provinces require the payment of drivers' licence fees in addition to income from the certificate of insurance premium. These fees are largely based on surcharges related to the demerit points on the driving record. A basic drivers' licence fee is payable in both Manitoba and Saskatchewan, regardless of accumulated demerit points, whereas there is no fee payable in British Columbia if a driver's record is clear. As these fees are applied at the time of driver licence renewal, they apply to all drivers and not just to vehicle owners as under the private industry system of surcharging.

In Manitoba and Saskatchewan, a gasoline tax of 2 cents out of a total gasoline tax of 18 cents and 3 cents out of a total 19 cents per gallon respectively is set aside for the government insurance corporation and is added to

underwriting revenue. A similar provision in the B.C. Automobile Insurance Act for a 10 cent per gallon tax for insurance purposes has not been utilized. Both the gasoline tax and the drivers' licence fees are applied equally to all rating classes to reduce the amount of compulsory insurance premiums payable by vehicle owners.

The gasoline tax in particular is a method of collecting revenues that is at the discretion of the government in power in the Province. The gasoline tax is regarded by some as "hidden" taxation that prevents taxpayers from ascertaining what is happening to their money; it is however acknowledged to be a simple method of collecting automobile insurance revenue. If government policy were changed to eliminate the gasoline tax, government underwriters in Manitoba and Saskatchewan might be forced to revise premiums upwards.

The government corporations also apply investment earnings and operating surpluses to the underwriting income base when establishing rates. This measure minimizes the amount of premiums contributed by motorists. In effect, private industry follows the same practice to the extent that it relies on investment income as a second source of income that is eventually considered in evaluating an insurance company's premium requirements.

Surcharges and Discounts

Both Saskatchewan and Manitoba apply an additional accident surcharge in the case of accidents for which the driver is 50% or more responsible. British Columbia does not impose this penalty. These accident surcharges, combined with the offence record surcharges paid as a driver's licence fee, penalize the driver "after the fact" for careless driving. These penalties are the means used in Saskatchewan and Manitoba to impose a heavier premium burden on the careless driver, as the basic system of rating does not generally take into account "in advance" the likelihood of being involved in an accident based on detailed characteristics of the driver and vehicle use.

The rating system in British Columbia is similar to that in Ontario in that it imposes premium penalties for high risk classes of drivers "in advance" of an accident. However, I.C.B.C. has developed an incentive system of safe driver discounts to redistribute excess premiums in a manner which lowers the cost of insurance to the good driver. This incentive system is described further in Appendix A.

Summary

In summary, underwriting by a government insurance corporation may differ from the present practices of a private company in the following ways: risk selection and "creaming" is eliminated because the government insurer

must accept all risks; a uniform classification system is applied to all insureds; additional sources of income can be tapped to lower premiums, reduce deficits or provide safe driving incentives; and cross-subsidization of risk classes can be carried out to achieve perceived social goals.

As the preceding discussion shows, the cost of the insurance product is not distributed in an identical manner through the rating policies of the government insurance corporations under study. Each has its own individual rating classification system: in the two Provinces of Manitoba and Saskatchewan broad risk classes are maintained for compulsory coverage while in British Columbia a more traditional classification system is retained. In addition each government insurer varies somewhat in its approach to collecting income from sources other than insurance certificate premiums.

2. Administration of Funds and Use of Profits

With government ownership, there is an opportunity to establish direct responsibility and accountability to the motoring public. The head office and the entire organization are resident in the Province. There is a legal obligation to administer the operations of the insurance corporation in the interests of the insurance buying public of that particular Province. This section examines how the government ownership Provinces administer their automobile insurance funds and how they invest their surplus monies.

The Automobile Insurance Fund

The provincial insurance corporations administer both a compulsory and an optional insurance programme that is funded through payments from the drivers and owners of motor vehicles in each Province. The insurance programmes of the government insurers are, in general, accounted for under a separate fund created by the respective Automobile Insurance Acts.

In Manitoba and British Columbia, the automobile insurance fund is credited with income from premiums from both compulsory and extension coverages, together with revenues from other sources and with interest earned on investments, and is charged with the costs of claims, commissions and operating expenses, including start-up and development costs which are being amortized over a fixed period of years. A separate and distinct accounting system is maintained for the general insurance divisions of M.P.I.C. and I.C.B.C.

In Saskatchewan, premium and other income, claims costs, and operating expenses resulting from compulsory automobile coverage are accounted for separately from that arising from optional coverages also sold by S.G.I.O. Funds collected from optional extension policy premiums form part of the general revenue of the Saskatchewan Government Insurance Office along with premiums from fire, casualty and other general insurance

lines. Investment income is allocated between compulsory and general operations.

Use of Profits

In all three Provinces, surplus revenues resulting from operations are retained in the automobile insurance fund and are used to increase benefits, reduce premiums or absorb deficits. Profits earned from compulsory automobile insurance may not be appropriated by the government for other uses.

All surpluses from both underwriting revenue and investment earnings are allocated to the automobile insurance funds and the government corporations control the use of investment funds, subject to some control by the respective Ministers of Finance. Lending is concentrated in each Province to the fullest extent possible. For the most part, the investment monies generated by the automobile insurance funds are not considered to be significant in their contribution to *total* investment activity in the respective Provinces.

S.G.I.O. and M.P.I.C. invest available funds mainly in provincial, hospital and municipal bonds and debentures. In British Columbia, it is currently corporate policy to invest most of the available funds in short-term securities, with maturities ranging from one day to one year. Investment income in 1976 ranged from 5% to 8% of the total revenues collected under the automobile insurance funds in the government ownership Provinces.

Summary

In general, the government insurance corporations are in a position to establish a framework from which to administer funds in the interests of the consumer or the community. To date surplus revenues have generally not been used to increase Accident Benefits levels nor have they been of major significance in funding programmes or investments outside the insurance sector. However, profits on compulsory coverage are retained in a separately administered fund and have been used to reduce premiums, as in the case of the I.C.B.C. safe driver discounts; to reduce deficits; and to fund programmes, such as automobile research centres operated by S.G.I.O. and I.C.B.C.

3. Marketing and Delivery System

Introduction

The government automobile insurance corporation has the opportunity, without concern for the competitive consequences, to implement a marketing system that is significantly different from that of the private insurance company. In the first place, the government corporation can change certain

of the characteristics of the product it offers to reduce the costs of delivery. For example, it can simplify the rate classification system and standardize coverage to permit a simplified transaction process. Secondly, the government insurance corporation can offer insurance as a joint product that is tied to the delivery of a legally required document, such as the driver's licence or the motor vehicle registration plate or card. Finally, it can alter the selling function and the distribution system. For example, it can change the procedures of its sales agents and it can make some use of publically operated facilities, such as the local motor vehicle branches, for delivery of its product.

The objective in all cases is to ensure universal availability of the product, and secondly, to reduce the high selling costs associated with the traditional private industry marketing system. It is, however, important to note that reduction in selling costs may not always be in the best interests of the consumer. Part of the selling function may be to explain the product to the consumer so that he can make an intelligent purchase suited to his individual needs. The nature of the product and the options available determine the relative importance of this function.

The nature of the insurance product and the delivery system in the government ownership Provinces, including the role of the agent and its effect on selling costs, are examined individually within each Province in Appendix B. General remarks are outlined below.

The Product

Evidence of basic insurance in the three government ownership Provinces is provided by the Vehicle Insurance Certificate. Motorists do not receive a copy of the policy and presumably receive instead the benefits of the savings that result when the provincial corporation is not required to print, file, endorse or retrieve policy forms. On the other hand, the failure to receive a copy of the policy may result in a lack of consumer awareness of the rights and benefits conferred under the policy.

The Manitoba and British Columbia insurance systems provide evidence of both basic and extension coverage under one proof of insurance certificate, which is the same document as the motor vehicle permit. The Saskatchewan system does the same for compulsory coverage but issues a second separate certificate if extension coverage is bought from S.G.I.O.

To facilitate the financing of the purchase of compulsory coverage, both Manitoba and British Columbia provide an instalment plan. Saskatchewan does not, without any apparent demand for one from consumers. However the instalment plan creates a bad debt problem for Manitoba and British Columbia and the need for the Motor Vehicle Board (M.V.B.) to assign staff to the seizure of licence plates in the event of non-payment of monies owed. The problem is not considered to be significant.

The Delivery System

All of the provincial automobile insurance corporations in Canada tie marketing of insurance coverage to the issue and renewal of the licence plate. A vehicle licence cannot be obtained without purchase of basic insurance coverage. In addition, failure to pay licence premiums or surcharges invalidates insurance coverage and results in non-renewal of the driver licence. A plate-to-owner system of licencing readily facilitates this link-up of the marketing of insurance to registration renewal.

All three government insurers have also established a close liaison with the Motor Vehicle Licencing Board. They use the facilities of the local motor vehicle licencing branch, to a greater or lesser degree, to market their insurance product. Furthermore, they utilize the infraction or driver records maintained by the Motor Vehicle Board as an input to the demerit-point system of surcharging.

With the linkage of insurance to motor vehicle registration, the transaction activity during the registration renewal period is significantly increased. In Manitoba and in British Columbia, transactions continue to be concentrated around a fixed annual renewal date. Saskatchewan has made the move to staggered renewals recently and British Columbia plans a similar move, but the costs and organization required have resulted in delays in implementation.

While the compulsory insurance package is sold through the licencing system in all three government ownership Provinces, purchase of extension coverage need not be tied directly to the licencing system. In Manitoba and British Columbia, the Autopac or Autoplan agent is also an agent for the licencing branch such that registration renewal, compulsory insurance transactions and the extension insurance transactions can be carried out at one time. In Saskatchewan, on the other hand, only about one-quarter of insurance agents are also agents for the licencing system and therefore the purchase of full insurance coverage is more likely to involve a two step process. In all three Provinces, purchase of insurance coverage may also involve a two step process if extension coverage is bought from a private insurer.

The Role of the Agent

Given this structure of the delivery system, the role of the agent in the marketing process has been altered in the government ownership Provinces. The agent, although working under revised procedures, is an integral part of the marketing mechanism of the provincial corporation for both compulsory and extension product lines in Manitoba and British Columbia, and for extension coverage in Saskatchewan. The agent relies almost totally on transaction of business for the government insurer for the automobile segment of his business.

The position of the agent in Manitoba and British Columbia remains relatively secure as long as the consumer continues to buy his insurance through the agent rather than directly from the government insurer or from motor vehicle branches; and as long as the general insurance market remains relatively competitive. At the present time, about 85% of automobile insurance transactions are carried out by agents and only 15% through motor vehicle branches or other direct means. However, in Saskatchewan, where only one-quarter of the agents are licenced to issue both compulsory insurance and registration certificates, the role of the agent could be severely curtailed if an increase in compulsory coverage limits were to reduce the size of the extension coverage market.

Government ownership has changed certain of the functions of the agent. Agents no longer deal with policies and no longer incur high mailing charges for policy renewals or changes. They no longer have accounts receivable or bad debt problems because the government insurer assumes full responsibility for collection of debts. Most agents in British Columbia and Manitoba, and a good proportion in Saskatchewan, earn additional income for processing registration renewals. Still, the agent remains a vital intermediary for many consumers, providing advice on levels of coverage, on available options from both government and private insurers, and sometimes on the procedures to follow in filing a claim.

Selling Costs

The government insurers maintain that the commission rate structure they apply to agents reflects the altered role of the agent. Services rendered in selling compulsory coverage, which requires no sales effort on the part of the agent or licenced issuer, are paid for on a flat fee per transaction basis in Saskatchewan and British Columbia, and at the low rate of 5 percent of the premium value in Manitoba. The commission on extension coverage is paid on the higher percentage basis of 17.5 percent in Saskatchewan and 10 percent in both Manitoba and British Columbia, in some part to provide an incentive for agents to sell the extension policies of the government insurer, since private insurers are competing in this segment of the market. However, the relatively low premium value of extension coverage, especially in Manitoba and Saskatchewan, where vehicle damage is part of compulsory coverage, serves to reduce the dollar value of the commission to the agent to a relatively low amount per transaction. The equity of the commission fee in British Columbia has recently been examined in an independent study which will form the basis for negotiation of commission rates for the 1978 fiscal year.

Without commenting on the equity of the selling fee structure in the government ownership Provinces, it is evident that the purchaser of automobile insurance can expect that a lower percentage of the premium burden that he pays to the government insurer will be used to pay direct selling costs.

Table 9 in Section E illustrates this point further. On average in Ontario, commission expense accounts for about 14 percent of premiums earned; in Manitoba average commission expenses account for roughly 4 percent of premiums earned, in Saskatchewan for 3½ to 4½ percent, and in British Columbia for about 8 percent.

Competition from Private Insurers

The present governments of British Columbia and Manitoba have expressed the desire for more private industry competition in the extension coverage part of the automobile insurance market in order to establish benchmarks for analyzing the productivity and efficiency of the government corporation. However, the tied marketing of compulsory and extension coverage, the lower direct selling and administrative costs of the government insurance carrier, and the high expenses in relation to the low premium value of the extension policy have made it very difficult for the private insurance company to compete with the government insurer. The government insurer, in effect, sets the price for extension insurance in each of the three government ownership Provinces and private companies are forced to meet this price to remain competitive.

As a condition for returning to the British Columbia market, private industry is demanding open competition for both compulsory and extension coverage. This move would expand the premium base for the private companies and thereby facilitate a broader distribution of their expenses. However, even in the case of an open market, the private insurers are still likely to find it difficult to compete: competition will eliminate some of the advantages of the one-company system, but the government insurer might continue to enjoy the benefits of its own established claims centres, computerized policy handling procedures, linkage with the licencing system and, particularly, its access to other sources of income such as the gasoline tax and drivers' licence fees. Assuming that these factors contribute to lower product prices, changes might be required to provide financial incentive for private industry to return.

Summary

In general, the government corporations have simplified the form of the insurance product by the issuance of an insurance certificate that is part of the vehicle registration certificate. Secondly, they have simplified the delivery system by integrating it with motor vehicle registration renewals. Corresponding reductions in agents' remuneration have been achieved. As a result of the restructured marketing system, the "outside" sources of income, and the changes in claims handling procedures described in a following section, it has become unattractive for private insurers to compete in those segments of the market that are open to them.

4. Enforcement of Compulsory Insurance

The three government ownership Provinces integrate the insurance carried on a vehicle with the licence plate. This integration involves a change from the previous system in which the licence plate remained with the vehicle regardless of ownership, to one in which the licence plate remains with the owner and may be transferred from one vehicle to another. The plate-to-owner system results in the near certainty that as long as a valid licence plate is attached to a vehicle, then the vehicle is covered by at least the basic required insurance.

With a plate-to-owner system, an opportunity to have a non-cancellable policy system has been created in the government ownership Provinces. In order to cancel a policy and obtain a refund a motorist must take the plates off the vehicle and turn them in. The government insurer also has the authority to cancel under certain conditions, but must in such a situation make arrangements to collect the vehicle plates. Accordingly, non-payment of monies owing for premiums generally becomes a bad debt question, not necessarily a question of cancelling the policy. Manitoba provides a 30-day grace period for unpaid premiums under the instalment plan, after which insurance is cancelled and plates are subject to seizure. The delinquent motorist is charged for the unpaid portion of his coverage when he renews his vehicle licence.

The linking of insurance to the licence plate provides the only truly effective means of enforcing a compulsory insurance law. Under such a system the only uninsured situations are stolen vehicles, out-of-province uninsured motorists or someone switching plates to a vehicle that is not properly registered. The incidence of these cases is minor in the three government ownership Provinces.

In all three Provinces, the police follow the practice of checking for lapsed renewals resulting in expiry of insurance coverage when spot checks are being conducted. There is no other regularly applied method of enforcement, although some effort is given to collection of licence plates in the case of unpaid premiums.

Further discussion of compulsory insurance and methods of compliance and enforcement is provided in Chapter 25 of the Committee's First Report on Automobile Insurance and in Part I of this Report.

Summary

In general, compliance with compulsory insurance is more difficult to enforce under the private sector, given the greater complexity of transactions within a multi-company system, than under a one-company system of government ownership.

Furthermore, government ownership facilitates the *effective* linkage of

the insurance and licencing systems through close coordination with the operations of the Motor Vehicle Board. This close liaison may not be as readily established under a private industry system, unless a formula to allocate the costs of shared functions can be agreed upon by all companies.

5. Claims Handling and Settlement

The One-Company Concept

Government ownership permits the establishment of a one-company system of claims administration. Under the one-company concept many claims handling procedures are simplified. If a government corporation were to compete with private insurers for a large segment of insurance coverage, some advantages in the area of claims handling, as developed below, would not be fully realized or could only be accomplished in cooperation with all companies including the government insurer.

Under the one-company government ownership concept, there is an inherent opportunity for claims handling to be more efficient. The government corporation has the opportunity to deal directly with all claimants including third-party claimants, it is able to make significant improvements in the appraisal and adjusting processes, and it should be able to exercise better control over the costs of repairs.

It should be possible to serve the claimant better under a one-company system. The claimant in all cases deals with only one organization, and does not encounter the confusion in the claims settlement process that is often experienced in the private sector.

For example, the claimant is unlikely to be left to pursue his own claim. In the multi-company system, if a vehicle is damaged through the fault of someone who is insured by another company, the driver without collision coverage generally must personally prosecute his claim against the other motorist's insurance company. His own company often will take no action in pursuing this third-party claim. While in theory the same holds true under the government ownership system, both parties have the same insurer. As a result each driver applies to the same insurer to obtain recovery, including the deductible portion on the basis of agreed division of responsibility if such agreement can be reached.

Another advantage of the one-company concept lies in the potential for economies in the mechanics of the adjusting process. High claims costs which result from interaction and dispute among different insurance companies can be reduced under a one-company system. In addition, Saskatchewan, Manitoba and British Columbia have each adopted the claims centre concept as a method of processing claims. The advantages of the claims centre concept under a one-company insurance system are outlined

below, while a brief description of claims handling procedures and facilities in each of the government ownership Provinces is provided in Appendix C.

The Claims Centre

The drive-in claims centre under a one-company government ownership system serves a dual function: it acts both as an appraisal centre and also as a centre for claims settlement. A "claims centre" is a centre in which all phases of the adjusting process can be carried on under one roof: appraising the repair costs, recording the claim and deciding upon the claimants' entitlements. In contrast, an "appraisal centre" is a centre in which activities are substantially limited to appraising repair costs. The advantages of an appraisal centre have already been recognized by the Committee in its First Report.¹ Briefly stated they include:

- Claimants save the time and inconvenience that would otherwise be involved when the insurance company demands two or more competitive estimates of damage;
- Repair shops need not spend time on estimates for jobs they may never do;
- Garages receive payments more quickly by dealing directly with insurance companies on the authorization of the drive-in centres;
- The potential for abuse is reduced considerably. Repair costs can be controlled by centralization of the estimating function;
- Savings in adjusting costs are sometimes achieved, as adjusters in many cases are able to use the appraisal centre facility to inspect the damage or interview the claimant, rather than travel to the claimant's place of residence.

In a multi-company insurance system, the importance of the above benefits of appraisal centres must be recognized by a large number of companies and a method must be devised which will make it obligatory that all companies bear their share of the cost. The insurance industry in Ontario, for example, has already shown initiative in setting up appraisal centres.

A one-company system facilitates the quicker adoption of the appraisal centre concept and it further facilitates the coordination of the appraisal and adjusting functions. Under the private multi-company system, the appraisal and adjusting processes are currently carried out separately. Under the Insurance Bureau of Canada's Appraisal Centre system as it operates at present, only the appraisal process is routinely carried out in the drive-in centre. Although space may be provided for adjusters to work in, the adjusting process is performed by a multiplicity of insurance companies or independent adjusters and they cannot all be allocated space in the appraisal facility.

1. Select Committee on Company Law, *First Report on Automobile Insurance*, pages 141-2

Private insurers will need to reach agreement on the use of common adjusting staff, either independent adjusters or I.B.C. hired adjusters, before the adjusting function will be effectively linked under one roof to the appraisal function. In the one-company government ownership system, all adjusters are employees or agents of the provincial corporation and are accommodated together with the estimators in localities which have a claims centre. While the adjuster is getting the information he requires, an estimator can complete the appraisal.

Integration of the damage appraisal procedure with the adjusting procedure allows the claimant to process his claim in a single step. Furthermore, he has direct contact with the insuring organization: he is no longer required to deal with intermediaries, such as body shops, independent adjusters, or the agent from whom he bought his insurance.

Claims centres cannot be established in all localities, particularly when population density is low. Therefore, the government insurers continue to rely on staff adjusters and independent adjusters to service small towns and rural areas. However, in those areas where distances permit, bringing the adjustment and claims handling process into local drive-in claims centres provides the potential for the following substantial improvements in the adjustment process:

- Adjusters are not required to travel to the claimant, saving time and expense;
- Claims can be processed prior to vehicle repair, as estimates are provided concurrently with the adjustment process;
- Records, comparisons and the counsel of senior personnel are readily available at all times to aid in the adjusting process;
- Access by means of data communications systems can be provided to the Vehicle and Driver Files of the Motor Vehicle Board to aid in the matching of accident and claims files.

In summary the ability to tie appraising and adjusting together within the claims centre is made easier under a one-company system. Government ownership also provides a close liaison with the provincial Motor Vehicle Board to aid in developing records and data processing systems that speed claims settlement. Similar progress in improving claims handling can be made under a private multi-company system, but the practical difficulties of organization are greater and the possibilities of some companies benefiting more than others are an obstacle to cooperation.

Claims Experience

a) Distribution of Claims by Type

Table 7 below illustrates the distribution of claims by type in the three government ownership Provinces, compared to Ontario claims experience.

TABLE 7
DISTRIBUTION OF THE DOLLAR VALUE OF
INCURRED CLAIMS BY TYPE OF COVERAGE

	Ontario 1975	Manitoba 1976	Saskatchewan 1975-76	British Columbia 1976-77
	%	%	%	%
Bodily Injury Liability	34.3	16.7		36.2
Physical Damage Liability	26.6	14.7	10.3	28.4
Death Benefits	0.7		1.5	1.2
Accident Benefits	4.9	4.6	3.4	4.2
Collision ^a	25.9	52.6	61.6	24.1
Comprehensive	7.6	11.4	5.1	5.9
	100.0	100.0	100.0	100.0

^a Compulsory in Saskatchewan and Manitoba (with \$200 deductible).

Source: Insurance Bureau of Canada, S.G.I.O., M.P.I.C., and I.C.B.C.

The distribution of claims by type of coverage is very similar in British Columbia and in Ontario, indicating that government ownership apparently has not affected the distribution of losses by type of coverage. However, Saskatchewan and Manitoba show a significantly different distribution of claims. Claims under liability coverage are greatly reduced as a percent of the total. A large part of this difference may be attributed to the mandatory provision for collision coverage which eliminates a large measure of third-party property damage claims.

Bodily injury claims, under Accident Benefits and death benefits coverage, are not appreciably different in percent of total in the four Provinces studied. However, liability claims for bodily injury assume a much lower percentage of the total value of claims in Saskatchewan and Manitoba compared to Ontario and British Columbia. As no differences in severity of accidents are readily apparent in these two Provinces, it would appear that the lesser weight given to bodily injury claims may be due again to a greater volume of property damage claims created by the compulsory requirement for collision coverage.

b) Extent of Litigation

Little information is available regarding the litigation of motor vehicle claims under government ownership compared to the previous system under private industry. As already indicated in Section A, Manitoba, Saskatchewan and British Columbia officials indicate that under government ownership less than 1% of their total auto insurance claims reach court. In comparison, Ontario data indicate that about 2% to 3% of total claims go to court.

Since the introduction of I.C.B.C., litigation of motor vehicle cases is said to have assumed less frequency in British Columbia. Over the period March 1974 to September 1977, more than 8,000 civil actions were started

relating to auto accident claims, excluding small claims. In Ontario, over the shorter April 1974 to March 1977 period, close to 58,000 auto accident actions were started in the County and Supreme Court, seven times the B.C. rate, despite the fact that the incidence of accidents is only about three times higher.

The foregoing figures relate to claims that started in court. It is also relevant to consider the number of cases that actually continued right through to trial, that is, that were not settled or abandoned during the intermediate stages. During the period from March 1974 to September 1977 only 268 motor accident cases or 3% of actions started were tried in B.C. Over the period April 1974 to March 1977 about 7,000 motor accident cases or 12% of actions started were tried in Ontario. These figures appear to show that the incidence of motor accident litigation is very substantially lower in B.C. than it is in Ontario.

A one-company government ownership system appears to reduce the volume of litigation because it minimizes disputes over establishing liability for accidents. As there is only one insurer all claims are referred to the same organization. Assignment of responsibility is a matter that affects the blame-worthy claim record of the driver but does not entail an extended dispute by the insurer over who pays, as the public insurer pays in all circumstances. Instead, litigation is limited largely to disputes over quantum, that is, claims and offers that are widely apart, or over claims which exceed limits of coverage.

The government corporation realizes a saving by eliminating the subrogation function between insurers on property damage claims including collision coverage. As one company handles all claims there is no need to negotiate inter-company payments. In Manitoba and Saskatchewan, where collision coverage is mandatory, vehicle damage claims are paid directly to the motorists suffering the damage without regard to fault, exclusive of the deductible. As the claimant is no longer placed in an adversary situation, except in respect of his deductible portion, the importance of litigation in vehicle damage claims is minimized. Furthermore, litigation for the deductible portion may also be reduced, as in cases where agreement on responsibility is reached the government corporation pays the appropriate portion of the deductible that is payable under the third-party liability coverage of the blameworthy driver.

c) Claims Frequency

Numerous external factors contribute to claims frequency, including concentration of the vehicle population, geography, and weather. Of perhaps greater importance than these factors are lenient attitudes on the part of the adjusters which may result in unsubstantiated claims that can contribute to a high level of claims frequency.

TABLE 8
CLAIMS FREQUENCY

	1974		1975		1976	
	Number of Claims	Claims Per Registered Vehicle	Number of Claims	Claims Per Registered Vehicle	Number of Claims	Claims Per Registered Vehicle
Saskatchewan	97,100	.17	112,700	.18	120,400	.18
Manitoba	179,000	.35	175,000	.33	181,000	.33
British Columbia ¹	500,000	.37	614,000	.40	370,000	.23
Ontario ²	824,200	.22	836,400	.21	731,900*	.18

1. Distribution of claims per year in 1974 and 1975 is not considered to be representative of normal operations because of start-up and strike.

2. Passenger and commercial vehicles.

* Incomplete.

Sources: S.G.I.O., M.P.I.C., I.C.B.C.

Statistics Canada

Insurance Bureau of Canada, *Automobile Insurance Experience*, 1976

Table 8 indicates that the frequency of claims per registered vehicle appear to be disproportionately high in Manitoba and British Columbia. British Columbia in particular has experienced the tendency of a government corporation to be tolerant of fraudulent or exaggerated claims made by some members of the public. This tendency was encouraged by inexperienced adjusters and an overgenerous attitude during the start-up period of I.C.B.C. The majority of fraudulent claims were related to unwitnessed theft or single-car damage claims. A tougher and more knowledgeable attitude by claims adjusters, combined with the introduction of a special fraudulent claim unit, and perhaps also the threat of accident surcharges, has significantly reduced the number of such claims. Equally important, the switch from compulsory to optional own-vehicle coverage in mid-1976 has reduced the number of insured persons under collision coverage and the overall frequency of claims. The effect of these factors together with a lower rate of accidents was to bring down claims per registered vehicle from around .4 in 1974 and 1975 to .23 in 1976.

In Manitoba, relatively high claims frequency may be attributed in some part to the provision for compulsory collision coverage. Saskatchewan with its long history of government insurance shows no evidence of high claims frequency.

Summary

It would appear from the foregoing discussion that, in general, claims are settled expeditiously and fairly under the government ownership systems examined, despite the evidence of some problems such as the start-up difficulties experienced by I.C.B.C. and some complaints in Saskatchewan of arbitrary "50-50" settlements by S.G.I.O.

The simplified and efficient processing of claims is enhanced by the

claims centre concept adopted by the government automobile insurance corporation. A one-company system of claims administration also provides benefits by eliminating many of the costs of disputes between insurance companies. As a result, litigation of claims is said to have assumed less importance in the government ownership Provinces. Higher claims frequency appears to have been encouraged by government administration of funds in the start-up stages of the government corporations, as there appeared to have been a tendency for the claimant to take advantage of the public purse.

6. Administration And Other Aspects Of A Government Owned Corporation

The near monopoly positions of the government automobile insurers in Western Canada provide a number of advantages and certain disadvantages associated with a single administrative organization serving the entire provincial market. Several of these advantages and disadvantages are briefly outlined below, followed by a review of specific programmes facilitated by organization into a single corporation.

Ramifications of a Single Administrative Organization

A single administrative organization for automobile insurance reduces duplication of administrative functions and related overhead costs which may result when a number of separate insurance companies are involved in providing the same service. In addition, it permits economies of scale to operate in the delivery of the insurance product and in the related support services such as printing, records maintenance, and other acquisition costs.

A single administrative organization provides the opportunity to pool statistical information to assist in underwriting, loss prevention, and the structuring of new benefit packages. Uniform practices in collecting claims data and internal accounting data aid in analysis and provide better management information.

A one-company administrative system also facilitates the undertaking of research aimed at reducing the cost of repairing vehicles and it provides an ideal environment within which a significant safety research and loss prevention programme may be carried out. Consolidation of research efforts under one organization which is committed to encouraging safe driving and improved repair procedures should result in significant contributions to these goals.

The single administrative organization is also in a position to control repair costs or to undertake salvage operations which permit better utilization of used parts. For example, salvage operations have been used in Saskatchewan to generate additional funds for the automobile insurance fund and reduce the cost of losses.

These advantages must be weighed against the possible significant disadvantages of a single organization. For example, there is a greater potential for inefficiency in management: inefficiency may not be evident if there are no competitors against which to compare the performance of the government monopoly corporation. Furthermore, introduction of the one-company system is a major undertaking and is likely to cause considerable operational start-up problems and related high costs. As the British Columbia experience has shown, a single administrative organization is vulnerable to labour problems and disruptions, particularly if employees are unionized. It is also vulnerable to public opinion and to the pressures of special-interest groups such as body shop operators and tow truck fleet operators whose interests may be against the larger interests of the motoring public.

A brief summary of a number of specific programmes facilitated by organization into a single corporation is presented below. A discussion of the methods of reinsurance follows.

Data Processing

The government automobile insurance corporations in Manitoba and British Columbia maintain or have access to computerized records of claims files, and driver blameworthy accident and infraction records. Manitoba provides these data on an on-line retrieval basis to its claims centres to facilitate in adjusting claims. The British Columbia system does not permit on-line retrieval at the present time, but instant data recall in the larger agents' offices and in the claims centres is planned as a major improvement in the near future. Saskatchewan is also planning to improve upon its current methods of data processing.

Repair Costs

S.G.I.O. and I.C.B.C. both operate automobile research centres which carry on training programmes for adjusters and estimators, and conduct research in respect of repair techniques, repair equipment and standards. Manitoba is watching their experiences with interest before considering the development of their own facilities in this regard.

The government corporations undertake to enter into agreements for independent outside services in order to establish uniform and known rates. For example, the Insurance Corporation of British Columbia arrived at agreements in 1976 with auto body repair shops to increase labour rates by 8% to \$20.00 an hour. Such agreements place the government insurance corporation in a difficult and sometimes conflicting negotiating position because it is expected to be equitable both to the supplier and to the motoring public. These agreements may also be unsatisfactory because they are said to level repair rates around the maximum allowable limit and hence reduce price competition.

Salvage Operations

All three government ownership Provinces are involved in salvage operations. In Manitoba and British Columbia, vehicles acquired by the respective corporations through loss settlements are sold by public auction or closed tenders to licenced auto wreckers and bonded dealers. In Saskatchewan, S.G.I.O. has established its own salvage operation with a Salvage Division that makes used automobile parts available to the public at large at reasonable prices.

Salvage operations provide a means of recovering a portion of the losses incurred. Recoveries from salvage depots ranged from \$2.2 million in Manitoba and \$3 million in Saskatchewan to \$5.4 million in British Columbia in the 1976 fiscal year. In Saskatchewan revenues from salvage operations (recoveries less all costs) are accounted for by the S.G.I.O. general office and are not included in A.A.I.A. results. In contrast, net proceeds of salvage sales (proceeds less direct costs) in M.P.I.C. and I.C.B.C. are credited in reduction of claims incurred and overheads associated with the salvage recovery system are accounted for as claims costs or expenses.

Reinsurance

There is no evidence to indicate that, under private ownership, the flow of reinsurance funds outside the three Provinces was a problem that required government intervention. The government insurers, in the same way as private insurers, are faced with the option of either reinsuring or maintaining their own internal reserves for major losses. The reinsurance policies of the three government ownership Provinces are as follows.

The Saskatchewan Government Insurance Office does not reinsure for policies under the compulsory coverage programme; instead adequate reserves are maintained internally. In the event of a claim for serious and prolonged disability, a reserve is set out in the year of loss. S.G.I.O.'s extension coverage is reinsured on world markets. S.G.I.O. has not experienced any particular difficulties with reinsurance, but has commented that the British reinsurance market finds it difficult to separate Canadian experience from U.S. experience,—a universal problem for Canadian insurers.

The Manitoba Public Insurance Corporation self insures for basic and extension coverage and for some part of catastrophe coverage. A major portion of catastrophe protection has been and will continue to be obtained on the world reinsurance market, but premiums assessed for such coverage are becoming very high. As a result, M.P.I.C. is establishing its own reserve fund as a substitute for reinsurance. It is hoped that the premiums saved by not reinsuring and the interest earned by the reserve fund can be applied to the benefit of the automobile insurance programme.

M.P.I.C. has continued to reinsure some of its automobile risk under an agreement with the general insurance division on the basis of a fixed premium deposit with adjustments to be made based on experience. The amount of automobile insurance premiums ceded to the general insurance division for 1976 amounted to \$456,000.

The Insurance Corporation of British Columbia follows a policy of reinsuring of its automobile coverage, both basic and extension, by purchasing reinsurance coverage for losses in excess of \$750,000 up to \$10 million for one policy. In addition to this, I.C.B.C. has catastrophe coverage for an additional \$10 million for more than one policy. Reinsurance is obtained on a worldwide basis and I.C.B.C. has not experienced any difficulties with respect to its purchase.

7. Summary

This section has outlined the revenue sources, programmes and operating methods of the government insurance corporations. It is evident from the foregoing that there is some diversity in the approach each provincial corporation takes in the provision of the automobile insurance product and in the settlement of claims. A generalized consolidation of the advantages and disadvantages of government ownership for the functional areas examined in this section would, however, be inappropriate as it would omit many other important ramifications of a government operation. Accordingly, a summarized review of the various advantages and disadvantages identified in this study is deferred to Section G.

Nonetheless, the discussion in this section indicates that savings in the methods of marketing, claims handling and administration would be expected under government ownership, as a result of the economies of scale and the near monopoly position of the government automobile insurance corporation. The preceding discussion also indicates that government ownership facilitates a reorganization of certain functions to new methods of operation, as illustrated by the integration of the marketing function with the motor vehicle licencing system; and permits the collection of revenues in ways not open to private companies, such as through gas tax revenues.

The disadvantages of a government operation are however less evident in the foregoing discussion largely because the near monopoly positions of the government corporations eliminate the possibility of direct comparisons between operations of competitive insurers marketing in the same insurance environment. In effect, this factor of near monopoly and the restricted freedom of choice for the consumer is often cited as one of the major disadvantages of government ownership.

TABLE 9
AUTOMOBILE INSURANCE—
OPERATING COST STATISTICS OF THE
GOVERNMENT INSURERS AND THE ONTARIO INDUSTRY
(000,000's)

	Ontario Industry* (1971—1975)		M.P.I.C. 1972—1976)		S.G.I.O. (1972—1976)		I.C.B.C. (1974—1976)	
	Average	%	Average	%	Average	%	Average	%
Premiums Earned**	\$550.7	100.0	\$56.6	100.0	\$46.3	100.0	\$246.6	100.0
Claims Incurred	378.3	66.2	49.5	87.5	42.1	90.1	224.9	91.2
Claims Costs	46.7	11.0	4.5	8.0	3.7	8.0	17.3	7.0
Commission Expense	77.3	14.0	2.4	4.3)			19.8	8.0
Premium Taxes	11.5	2.1	1.2	2.1)	2.0	4.3	N/A	—
General Expenses	81.0	14.7	2.2	3.8	3.1	6.7	34.5	14.0
Investment Income	(52.0)	(9.4)	(2.4)	(4.3)	(4.1)	(8.9)	(14.4)	(5.8)
Total Expenditures	542.8	98.6	57.4	101.4	46.8	100.2	282.1	114.4
Profit (Loss)								
Before								
Income Tax	\$ 7.9	1.4%	\$ (.8)	(1.4)%	\$ (.5)	(.2)%	\$(35.5)	(14.4)%

* The Select Committee on Company Law, *First Report on Automobile Insurance*, page 190.

** Premiums earned in Ontario include all sources of income other than investment income; in Manitoba and Saskatchewan, premium income, drivers' licence fees and surcharges, and gasoline tax; in British Columbia, premium income and drivers' licence surcharges.

E. FINANCIAL RESULTS AND COMMENTARY

This section is intended firstly to provide a description of the financial history and specific operating considerations of the three government automobile insurance corporations, in order to identify factors which might contribute to operating differences in comparison with private companies. Secondly this section examines efficiency in the government corporation as compared to private companies.

1. Comparative Operating Results

Because of differences in the product itself and in the product mix, the following operating cost comparison should be regarded as a rough approximation only, intended to provide further background on the government insurers. In addition, comparisons with the Ontario industry are provided only to highlight possible opportunities for cost savings which may be forthcoming from government ownership, as described in earlier sections of this study.

Table 9 sets out an approximate calculation of the "average" operating results on a comparative basis of the three government insurers for the periods indicated. These results are compared to the Ontario industry "average" as set out in Chapter 27 of the Committee's First Report.

These calculations were prepared from the government corporations' published annual reports as certified by the auditors of these corporations. The accounting practices of the government corporations vary somewhat with respect to categories of expense and their allocation. Wherever readily apparent, appropriate adjustments or estimations have been made to improve comparability; however, this comparison should not be construed to be totally accurate. *Premiums earned on Table 9 include all revenues earned by the government corporations including automobile insurance premiums, drivers' licence fees and gasoline taxes where applicable. All operating expenses are shown net of recoveries from other government departments pursuant to cost-sharing agreements which are also subject to audit.* Other significant factors to be considered in examining Table 9 together with comments provided by the auditors of the government insurance corporations are outlined below.

Saskatchewan Government Insurance Office

1. S.G.I.O. operating results as shown disclose only the results of the basic compulsory coverage provided through the A.A.I.A. The results on the operations of the extension coverage are accounted for separately by the Corporation and are included with their general insurance operations.
2. Premiums earned, as shown on Table 9, include gas tax revenues which provided approximately \$28,000,000 in revenues in the years 1974 through 1976.
3. Officials of the S.G.I.O. concur that the resultant ratios of premiums to expenses are approximately representative of "normal" operations with respect to those activities provided by the A.A.I.A.
4. The Provincial Auditor in Saskatchewan in discussions with the Committee's consultants indicated that he had never been satisfied with the allocation of costs between the S.G.I.O. general insurance operations and the automobile insurance operations. In his opinion, there has been a definite tendency over the years to overload the A.A.I.A. operations with costs in order to improve the apparent results of the general insurance operations and he has expressed this opinion to S.G.I.O. management who disagree with it. He speculated that Saskatchewan drivers will pay increased auto insurance premiums without question but that S.G.I.O. general insurance rates must be competitive with private insurers; hence many subsidies have been made in that direction. He cited the example of 1972 and 1973 when he qualified his audit report because of his dissatisfaction with cost allocations between automobile and general insurance.

Based upon detailed calculations by his staff, allocated costs to the A.A.I.A. in those years were overstated by approximately \$3.5 million. In 1972 alone, S.G.I.O. reported a profit of \$300,000 on general insur-

ance operations and the Provincial Auditor is on record with his opinion that these results should have shown a \$1,500,000 loss; accordingly the A.A.I.A. was overcharged by \$1,800,000 in expenses.

The Provincial Auditor in Saskatchewan was less than emphatic in his opinions about possible hidden subsidies. While he indicated that he did not know of any subsidies, he acknowledged that they might exist. He was not aware that S.G.I.O. does not pay for the cost of police reports and medical reports.

Manitoba Public Insurance Corporation

1. M.P.I.C. statistics include the results of both the basic compulsory coverage and the optional extension coverage provided by the Corporation. Officials of M.P.I.C. agree that the resulting ratios of premiums to expenses are approximately representative of "normal" operations and are considered desirable targets for future operations.
2. On April 1, 1973, M.P.I.C. assumed responsibility for the motor vehicle licencing system. Recoveries from the M.V.B. on commissions (\$2.7 million) and general expenses (\$6.7 million) are reflected in the average statistics. These recoveries are negotiated annually and paid according to a formula agreed to by M.P.I.C., the Motor Vehicle Board, and the Provincial Auditor.
3. Premiums earned, as shown on Table 9, include gas tax revenues which provided approximately \$10 million of revenue in 1975 and 1976.
4. General expenses include the amortization of start-up costs, ranging at about \$235,000 per annum.
5. The Provincial Auditor in Manitoba has indicated to the Committee's consultants that he is well satisfied that the operating costs of the automobile insurance operations of M.P.I.C. are properly accounted for and allocated between the auto insurance fund and the general insurance operations and the activities of other government departments.

The Provincial Auditor further indicated that he had recently been asked about hidden subsidies by the Public Accounts Committee of Manitoba. He responded that the M.P.I.C. financial statements disclosed all costs and that he knew of no material omissions. He felt that M.P.I.C. was a "stand alone operation" and that it was "paying its own way".

As far as indirect benefits to M.P.I.C. were concerned, he cited as an example a Department of Highways advertising campaign in connection with speed limits which might be of benefit to M.P.I.C. No attempt was made to measure these types of benefits.

He knew of no "free rides" which might be available to M.P.I.C. and indicated that to the best of his knowledge, "economic values" were charged for all major items of operating expense.

Insurance Corporation of British Columbia

1. I.C.B.C. statistics include the results of the basic compulsory coverage and the optional extension coverage provided by the Corporation. I.C.B.C. officials do not feel that the average results presented are representative of "normal" operations for the future, because each of the years 1974, 1975 and 1976 had some unusual distortion: 1974/75 was the first year of operation with the associated start-up problems and 1975/76 had a 3½ month labour dispute with many activities and expenses which carried over into 1976/77.

Accordingly, they have provided the following ratios for each year which are presented on the basis of "break even" premium levels. Investment income is ignored in this presentation.

	1974/75	1975/76	1976/77	Target
Claims Incurred	81.5%	78.2%	68.8%	78.5%
Claims Operations Expense	4.6	5.3	7.4	6.7
Administration Expense	6.6	9.4	10.4	9.7
Agent's Commission	5.7	5.6	8.7	5.1
Sub-total	16.9	20.3	26.5	21.5
Start-up Amortization	1.6	1.5	4.7	—
Total Expenses	18.5	21.8	31.2	21.5
Total Claims and Expense (Net Premiums Earned)	100.0%	100.0%	100.0%	100.0%

2. The operating costs of I.C.B.C. include amounts that are directly related to the issuance of licence plates on behalf of the M.V.B. The Corporation may be reimbursed for such expenses in the future.
3. Large losses incurred by I.C.B.C., in its first two years of operations (\$178 million) were funded by a grant from the provincial government.
4. Representatives of Deloitte, Haskins, and Sells, the independent auditors of I.C.B.C., indicated to the Committee's consultants that they were well satisfied that proper and fair allocations of all reported operating costs had been made between the automobile insurance operation and the operations of the general insurance division and other government departments. They further stated that great care had always been taken to ensure that all costs were included in I.C.B.C. results. For example, all salaries and fringe benefits of civil servants on loan to I.C.B.C. from other government departments were allocated to I.C.B.C.
5. The auditors of I.C.B.C. stated that they knew of no hidden subsidies which might be available to I.C.B.C. nor were they aware of any instances where "economic values" had not been charged for services provided to I.C.B.C. They stated that they would be very surprised if any hidden subsidies did exist because of the constant political scrutiny to which I.C.B.C. had been subjected since its inception.

Corporate income taxes are not considered in Table 9, because the public insurers as government corporations are not required to pay income taxes and because their stated objective is to break even on operations. However, non-payment of corporate income taxes could be considered to be a disadvantage of government ownership in that federal, and ultimately provincial, general revenues would be reduced by the corporation taxes presently being paid by private automobile insurers.

2. Comparative Operating Costs

It is extremely difficult to determine, with any degree of certainty, the actual amount of savings in operating costs which might be forthcoming through government ownership. In the preceding section of this study, the comparative operating results and commentary provide a background to the complexity of this problem. The practices followed and the results obtained by the government insurers themselves complicate individual comparisons. Differences in accounting methods, sources of revenue including access to subsidies, and taxation status only serve to compound this difficulty.

Recognizing these shortcomings, however, it was considered useful to quantify in very rough terms, the apparent spread of costs between the three government insurers and private companies in Ontario. In order to accomplish this, it was initially necessary to develop an average or theoretical operating cost structure for the government insurers which is shown on Table 10 below:

TABLE 10
GOVERNMENT CORPORATIONS—COSTS BY FUNCTIONAL COMPONENT

	M.P.I.C. %	S.G.I.O. %	I.C.B.C. %	Average %
Acquisition (including Premium Taxes)	6.3	6.5	7.1**	6.3
Underwriting and Policy Processing	1.7	3.6*	6.3	3.8
Claims Adjusting	7.9	7.4	6.2	7.2
General Administration	2.1	4.3*	2.5	3.0
Investment Income	(4.2)	(8.5)	(5.8)	(6.2)
<i>Total Operating Costs</i>	13.8	13.3	16.3	14.4
<i>Claims Incurred</i>	86.2	86.7	83.7	85.6
<i>Total Costs</i>	100.0	100.0	100.0	100.0

* General Administration allocated 45% to Underwriting and Policy Processing, as for M.P.I.C.

** No Premium Taxes in B.C.

This theoretical structure was prepared by converting the average results of the government insurers in percentage terms to a break even position, their stated objective, and then recomputing a new average for the three government insurers. Start-up costs were eliminated from the calculation in order to estimate the on-going operations only.

By the further allocation of general administration on an arbitrary basis, the estimated costs of the three major functional components of the system may be presented. These are outlined in Table 11 below and compared to similar costs estimated for the private industry system in Ontario as described in Report X by the Committee's consultants. Accordingly, the apparent spread may be calculated as follows:

TABLE 11
APPARENT SPREAD OF OPERATING COSTS
BETWEEN A GOVERNMENT INSURANCE SYSTEM AND
PRIVATE INDUSTRY IN ONTARIO

	Government System	Private Industry	Apparent Spread
Acquisition	8%	18%	10%
Underwriting and Policy Processing	5	8	3
Claims Adjusting	8	15	7
Total Estimated Operating Costs	21%	41%	20%

It is not realistic to expect that the above difference in operating costs could be saved by reorganization to government ownership nor does this apparent potential for savings imply that government ownership is the logical method of obtaining any savings perceived to be necessary in the Ontario automobile insurance industry today.

Government ownership embodies the "one-company" concept which does provide for certain savings by the mere fact that a government corporation is a monopoly and it does not incur costs associated with maintaining its competitive position in the market place. Also, the "one-company" operation provides economies of scale which otherwise would not be forthcoming. Short of a government monopoly therefore, it is impossible to expect that the upper limit for savings demonstrated in Table 11 could be achieved. Because of the very subjective nature of such a determination, no attempt has been made in this study to quantify the economies attributable to this feature of government ownership.

Such an analysis of operating costs does, however, permit some quantification of the differences in administration, delivery, and claims adjusting procedures which characterize the government insurance systems and are described at length throughout this study.

As evidenced by the foregoing sections, the accounting and cost allocation systems of the government insurers may not be as refined or sophisticated as might be necessary to determine unequivocally the costs of preparing, delivering, adjusting and settling their insurance products. The same situation is true of preparing detailed costs of the functional components of the system. In addition, the need to allocate costs between automobile and

general insurance operations and the existence of special cost sharing arrangements with other government departments such as Motor Vehicle Boards complicate the problems and perhaps lead to the allegation that true costs are camouflaged and/or that actual costs are offset by hidden subsidies.

Certain "free rides" likely *are* enjoyed by some of the government insurers. S.G.I.O., for example, does not pay for the cost of police reports or medical reports which could result in a sizeable saving over the course of a year. While this situation does not prevail in M.P.I.C. or I.C.B.C., the extent of these and other "hidden subsidies", if in fact they exist, is not readily determinable.

For the most part, the activities of the Provincial Auditors in Manitoba and Saskatchewan and the external auditors of I.C.B.C. should provide reasonable assurances that proper systems and cost allocation methods are employed, otherwise their audit reports would indicate material qualifications, as was the case with S.G.I.O. in 1972 and 1973.

Short of performing a detailed audit of the government insurers, the Committee's staff could not provide additional information which might refute the apparent spread in operating cost between the two systems.

3. Comparative Efficiency

A frequently accepted measure of the "efficiency" of an automobile insurance system is the percentage of the premium dollar that is distributed to the consumer in the form of claims benefits. In making comparisons between the various government insurance corporations, or between the government insurers and private industry, care must be exercised to ensure that *proper* comparisons of this "efficiency" factor are made. A superficial comparison of the percentage of the premium dollar distributed as claims benefits on Table 9 indicates a difference of 21.3% to 25% between the portion distributed by the government corporations in the West and that distributed by private companies in Ontario. Such a comparison, however, ignores two important factors in this instance: namely, the bottom line losses incurred by the government insurers which must be funded from somewhere; and the fact that S.G.I.O. statistics do not include the "average" results of its extension coverage experience.

In order to make a reasonably accurate comparison of efficiency, consider Table 12, which is prepared on the premise that an appropriate measurement of efficiency is provided when claims benefits are shown as a percentage of total expenditures. This comparison recognizes that, while differences exist in product and product mix, such differences should not impact on efficiency, but should be set aside as separate issues to be considered in evaluating the value of the protection and service provided to the

consumer. Accordingly, regardless of these differences, one may inquire what proportion of total revenues each system returned as claims benefits.

TABLE 12
COMPARISON OF CLAIMS INCURRED
TO TOTAL EXPENDITURES
(Based Upon Average Statistics)

	Ontario Industry (1971-1975) (\$ million)	M.P.I.C. (1972-1976) (\$ million)	S.G.I.O. (1972-1976) (\$ million)	I.C.B.C. (1974-1976) (\$ million)
Total Expenditures per Table 9	542.8	57.4	46.8	282.1
*Add Back Investment Income	52.0	2.4	4.1	14.4
Total Expenditures	594.8	59.8	50.9	296.5
Claims Incurred	378.3	49.5	42.1	224.9
Percent of Total Expenditures Returned as Claims	63.6%	82.8%	82.7%	75.9%

* To arrive at Total Expenditures.

** When adjusted to reflect extension coverage experience, produces an efficiency measurement in the range of 80%.
(See Appendix D)

Source: Table 9

The results of the comparison in Table 12 provide a better indication of the spread of total costs between the government corporations and private companies in Ontario as outlined in the preceding sections of this study. Representatives of the government insurers contend that a spread in the range of 18% to 20% is attainable.

As far as comparing the government insurers with each other is concerned, S.G.I.O. statistics must be altered to include the results of its extension coverage operations. As indicated in Appendix D, S.G.I.O. efficiency (claims benefits paid as a percentage of total expenditures) including extension coverage experience, appears to be in the range of 80%.

On the basis of this very rough comparison, M.P.I.C. appears to be the most efficient of the government insurers under consideration. Some reasons in support of this conclusion might be as follows:

- M.P.I.C. has progressed beyond the start-up problems recently being experienced by I.C.B.C. and has developed a reasonably sophisticated data processing system which appears to be significantly ahead of the state of the art at S.G.I.O.
- S.G.I.O. has indicated that it is currently modernizing its data processing and administrative systems which perhaps explains the higher general and administrative costs in this Corporation when compared to M.P.I.C.
- I.C.B.C. general expenses of 14% include approximately 4% for amor-

tization of start-up costs. This factor coupled with the fact that its large administrative plant is only now beginning to achieve operating efficiencies may explain its performance relative to the other government insurers.

Finally, it is important to note that many different measures can be applied to assess the efficiency of an automobile insurance system. Certainly a system which returns a high percentage of the premium dollar to claimants cannot be said to be efficient if, in so doing, it pays an excessive amount of fraudulent or inflated claims. Government insurers state that they have had problems in this regard on start-up but now are satisfied that these problems, for the most part, have been corrected. Similarly, an insurance system that delivers a faulty or inadequate product for a lesser cost cannot be said to be efficient if its product does not satisfy the needs of the vast majority of consumers. Little or no evidence has been uncovered to suggest that any major product deficiencies exist.

4. Summary

The operating results of M.P.I.C., S.G.I.O. and I.C.B.C. appear to support the conclusion that the government insurance system is capable of returning a higher percentage of its total revenue to claimants in the form of benefits. Total revenue includes insurance premiums, drivers' licence fees and surcharges, and gasoline taxes where applicable. The following factors contribute to this conclusion:

1. Because of its monopolistic nature, the government insurer need not incur those costs expended by a private insurance company to ensure the maintenance or expansion of its competitive market position.
2. As a result of economies of scale and major structural differences between the government and private industry systems, the government insurer experiences a lower level of administration and delivery costs.

Offsetting the above factors in some part might be a higher potential for inefficiency in some aspects of the government insurer's operations because of the lack of competition.

Considerable care should be exercised in the interpretation of the above conclusions. Differences in the product and the product mix and the possibility that the government organization may have some access to free services or cost sharing not available to private companies renders a definitive conclusion difficult. Also, the "low-cost" insurance certificate premium paid by consumers in the government ownership Provinces is somewhat of an illusion as it is only one of a number of sources of income used by the government insurance corporation to support the automobile insurance system. Differences in corporate income tax status encountered under the two systems and also the differences in personal income tax rates in the various

Provinces add yet another dimension to the evaluation of the ultimate relative positions of the consumer. As many measurements of efficiency are possible, a comprehensive evaluation of this matter is beyond the scope of this study.

However, on an overall basis from a consumer viewpoint, the government automobile insurance system appears more efficient than the private industry system to the extent that it returns a higher percentage of the total premium dollar. This conclusion is reached after all direct subsidies such as drivers' licence fees and gas tax revenues are included in premium income. Furthermore, no evidence has been uncovered by the Committee or its consultants which indicates that the above indicated higher return is the result of a continued abuse of the system; nor has the insurance product provided by the government system been found to be substantially inferior to that offered by the private companies in Ontario.

F. PUBLIC ACCEPTANCE

1. In the Government Ownership Provinces

Public acceptance of government ownership is probably most complete in *Saskatchewan*. S.G.I.O. and the A.A.I.A. have been operational since the 1940's and it appears that the public is complacent about government involvement in automobile insurance. There is no evidence to indicate that parties in opposition to the New Democratic Party Government of the day would initiate any substantial dismantling of the S.G.I.O. structure. The Liberal Government of Mr. Ross Thatcher reviewed the concept and operations of the S.G.I.O. and judged that the consumer's position could not be improved without considerable cost.

In Manitoba, where the M.P.I.C. was set up by a New Democratic Party government six years ago, the public appears to be satisfied with government automobile insurance. Although Autopac was not a campaign issue, when the Progressive Conservatives took over the government in October 1977, they announced their commitment to consideration of the possibility of opening Autopac and the government business of the general insurance division to competition. Private companies have subsequently expressed their interest in competing in these areas with the government plan.

Although no policy decisions have yet been made, it appears that the intention of the present government is to open up all government general insurance business to competition, to leave basic Autopac coverage solely with M.P.I.C., and to look at making extension automobile coverage more attractive to the private companies. The Highways Minister, The Honourable Harry Enns, who is responsible for M.P.I.C., has stated that "Autopac

has become an acceptable service to the public and the incoming administration recognizes this".¹

He also stated that Autopac is in a highly advantageous position from a rate setting point of view, because it has access to the two-cent-a-gallon gasoline tax and various surcharges on motor vehicle registrations and drivers' licences. A private insurer would not have access to these funds and would find it difficult to compete in the basic coverage market. Furthermore, he indicated that the government would not allow the private sector to "cream-off" the good risks, leaving the bad risks for M.P.I.C.

Pending the review of M.P.I.C. operations by the Progressive Conservative government, announcements by the previous N.D.P. government that Autopac injury benefits would be increased have not been acted upon.

The Corporation apparently cannot afford enrichment of Accident Benefits at this time, particularly as it has been suggested that the new government may repeal the 2 cent per gallon gas tax. However, the Corporation expects to break even in the 1978 fiscal year despite any possible loss of tax revenues. It further expects that it will be necessary to increase premiums for 1979 and it may be able to introduce some enrichment of Accident Benefits coverage at that time.

In British Columbia, a change of government from the New Democratic Party which introduced government ownership to the Social Credit Party has not resulted in any substantial reversal of government policy with respect to government ownership of automobile insurance. The Social Credit government did state in 1975 that private insurers should be given the opportunity to return to British Columbia, and in March 1, 1976, private insurance companies offering extension automobile coverage began to be licenced to sell in competition with I.C.B.C. In addition, collision coverage was switched back to an optional purchase system, expanding the size of the extension coverage market opened up to private companies. I.C.B.C. has nevertheless remained dominant in the extension market and private insurers have been reluctant to return so long as they must compete with I.C.B.C.

The current Social Credit government will not accept the dismantling of I.C.B.C. so long as it shows itself to be productive and efficient in its ability to serve the public. The Honourable Dr. P. L. McGeer, Minister of Education who is responsible for I.C.B.C., stated before the Committee during its investigation in Vancouver in September 1977 that it would be "counterproductive" to return to a complete private system because of the loss of efficiencies and the need to accommodate the residual market.

Dr. McGeer elaborated on his perception of the inherent efficiencies of a state-run automobile insurance system, including factors such as large

1. *The Winnipeg Free Press*, Friday, October 28, 1977.

market size, central data processing, claims centres, elimination of inter-company disputes, and the convenience to the insured of dealing with only one insurer.

The attitude of the general public towards government ownership of automobile insurance was tested by I.C.B.C. in a public opinion survey in which British Columbia residents were asked to compare I.C.B.C. to two other Crown corporations, B.C. Telephone and B.C. Hydro. Overall public acceptance was good, but certain segments, notably people in northern areas and the young driver under 25, were highly critical. The survey did not show any dissatisfaction with claims centres and it is believed that the initially critical public attitude, caused by significant start-up problems and the summer strike in 1975 by I.C.B.C. claims staff, has changed as more people go through the claims centres and come out impressed.

2. In Other Jurisdictions

The *Province of Quebec* has just recently made a significant move towards government ownership in the automobile insurance field. Legislation passed in December 1977 has established a governmental agency, the *Regie de l'assurance automobile du Quebec* (R.A.A.Q.), and entrusted to its administration a no-fault compensation scheme for bodily injuries caused by the automobile. The Automobile Insurance Act, passed also in December 1977 as Bill No. 67, further entrusts the Regie with the administration of a fund (*Fonds d'indemnisation*) providing indemnity to persons sustaining property damage caused by an automobile when the person responsible for damage is unknown, uninsured, underinsured or insured with an insolvent insurer.

Financing of the Regie and of the *Fonds d'indemnisation* will be derived from sums fixed each year by the Regie and paid by motorists for the issue of drivers' permits and motor vehicle registration certificates. The amounts set by the Regie are to be actuarially determined, based on payments to be made and related expenses incurred as a result of accidents that have occurred during preceding financial years.

The Province of Quebec has not at the present time established a government corporation to provide third-party liability insurance, which was made compulsory by the Automobile Insurance Act of 1977 for property damage and bodily injury outside the Province, or to provide own-vehicle damage insurance. These coverages continue to be provided by the private sector.

In order to ensure that every automobile owner is able to find a licenced insurer with whom he may take out third-party liability insurance, the 1977 Automobile Insurance Act also establishes a *Corporation des assureurs autorises* which must set up a mechanism capable of carrying out this mandate. The Corporation is composed of directors elected by licenced private sector

insurers, with votes weighed by their proportion of total gross automobile insurance premiums in the Province. The Superintendent of Insurance and one other person appointed by the provincial government are also required to attend the meetings of the board of directors.

A further mandate of the Corporation is to establish or certify appraisal centres for the appraisal of vehicle damage. Each licenced insurer is obligated to engage the services of the appraisal centre whenever possible and to share in the costs of their operation.

The Corporation must also establish a "direct compensation" agreement binding on all insurers that will reduce disputes between insurers regarding who is to pay. The direct compensation agreement would require the vehicle owner's own insurer to pay, under the third-party liability policy, for damages or for the deductible, based on a share of fault. The direct payment approach applies to all claims including cases where the driver has no collision coverage.

It is also the intention of the Act that the Corporation will establish or certify loss adjustment centres, standardize forms used for reporting accidents and adjusting losses, establish a centre to examine techniques of appraisal and repair, and provide information to the public. These are functions which are presently carried out by the government insurance corporations in Manitoba, Saskatchewan, and British Columbia.

The establishment of the Corporation will likely compell private insurance companies in the Province of Quebec to undertake many of the reforms and claims handling improvements that have been adopted under the one-company government ownership systems in Western Canada. The Automobile Insurance Act, however, permits the industry to determine how the Corporation should carry out its mandate. If private industry through the Corporation is unable to find a mechanism to solve satisfactorily the problems of the residual market and to cooperate in claims appraisal, the Parti Quebecois Government appears ready to consider the establishment of a government corporation in the property damage field, as well as in the bodily injury area.

In *New Zealand*, a compensation scheme for bodily injury resulting both from automobile and other accidents is administered by a public body, the Accident Compensation Commission, an independent statutory authority which has appointed the State Insurance Office as its claims handling agent. Property damage insurance, both third-party liability and collision coverage, is not covered by the Accident Compensation Act and is available on an optional basis from either the State Insurance Office or from private industry insurers.

In *Australia*, each state has its own State Insurance Office which provides compulsory third-party liability (bodily injury only) coverage, includ-

ing in some cases limited no-fault coverages. The State Offices also handle, on a voluntary basis, comprehensive vehicle insurance coverage which provides both third-party liability insurance for property damage and own-vehicle damage insurance. All of the State Offices compete with private industry for both types of coverage, with the exception of one state which excludes private industry competition for compulsory third-party liability insurance for bodily injury. The State Insurance Offices' share of the compulsory bodily injury coverage averages about 80% over all states; and their share of the optional voluntary coverage for property damage averages 35% and is growing.

Sweden's approach to the operation of automobile insurance is of related interest, since Sweden, a highly socialistic country, has considered and rejected nationalization. The Nova Scotia Royal Commission on Automobile Insurance reports:

"The basic reason that the insurance industry has not been nationalized in Sweden is that it is running efficiently. This is due to two main factors: centralization or concentration of the insurance companies controlling the major portion of business in the country; and the influence of the Cooperative, The Folksam Group. This organization's consumer-oriented policy and creative force tend to provide stiff competition for its conventional profit-motivated competitors."¹

Furthermore, the insurance companies in Sweden are controlled by a state authority, the Insurance Inspectorate, and their activities and their liability to policyholders are defined by legislation. In 1965, the insurance companies formed an Automobile Classification Committee to prepare a uniform classification system and later control of premium rating was assigned to the Insurance Inspectorate.

Given that the cooperative Folksam organization, through its competitive activities, exerts a beneficial influence over the automobile insurance industry in Sweden, and given that public intervention in the industry is already exercised through the Insurance Inspectorate, there appears to be little need for government ownership. On the contrary, it is generally felt that a nationalized insurance industry would not offer the same possibilities for direct consumer influence as does the cooperative Folksam Group. Secondly, it is felt that, in the event of nationalization, there would be a danger that a shift to a new government with new policies might adversely affect the nationalized operations.

1. Province of Nova Scotia, *Royal Commission on Automobile Insurance*, March 1973, page 280

G. CONSEQUENCES OF GOVERNMENT OWNERSHIP

1. Advantages

In random order, some of the perceived economic and social benefits attributed to government ownership are summarized below together with a brief commentary on the logic or the facts which support these claims. While certain of these factors may be duplications of others they are presented to serve as an "inventory" of various advantages outlined and discussed in the text of this study.

Benefits to the Motorists:

- reduced premiums from investment income and operating efficiencies.
- ideal environment for a significant safety research and loss prevention programme.
- research capability aimed at reducing auto repair costs.
- source of revenue to fund driver education.

Increased efficiency in terms of percentage of premium returned to the insured as claims benefits:

- one company, no adversary.
- claims handling and settlement restructured.
- reduced delivery costs.
- economies of scale.
- this efficiency is demonstrated in Tables 9 and 10.

No residual market and very small percentage of uninsured motorists:

- eliminates creaming and discrimination.
- solves availability problem.
- solution to the social problem of no insurance.

Head office resident in the province:

- social commitment to the province.

Utilization of investment income pool for in province investment:

- assist in accomplishing other social objectives.

Single accounting system and single claims experience:

- detailed specific costing could be achieved and the true costs identified and accordingly better controlled.
- improved visibility for future rate setting.

Cross-subsidization may be achieved within socially acceptable limits:

- improves affordability for the high-risk driver.

Highly effective means of compliance and enforcement of compulsory insurance:

- facilitated by link with licencing system
- more difficult to accomplish under private industry.

Public convenience:

- one stop shopping and claims adjusting.
- less confusion and misunderstanding on claims settlement.
- direct dealings with insurance company.
- opportunity for better consumer education.

2. Disadvantages

Some of the adverse consequences or disadvantages of government ownership are outlined below.

Impact on other forms of general insurance:

- possible capacity problems in the general insurance market if some insurers pulled out.

Possible illusions of low premium costs:

- low cost premiums may be only one of the methods by which motorists pay for insurance—they may be paying in other indirect ways such as the gas tax.

Impact on employment structure:

- reorganization to government ownership may disrupt employment in the insurance industry and cause job dislocation.

The government corporation does not pay corporate tax:

- loss of corporate tax revenues may need to be balanced through higher taxes in other areas.

Trend to inefficiency in management techniques, and operations because of lack of competition:

- lack of competitive sellers against which to judge the performance of the government insurer.
- M.P.I.C. managers are concerned about this and are attempting to develop specific mechanisms to ensure against it.
- need to “open up” to competition and difficulties associated therewith.
- tendency on the part of employees to satisfy customers from the “bottomless pit” of the government insurance fund.
- I.C.B.C. overly generous attitude which was subsequently changed.

Rating may become too simplistic or inequitable:

- S.G.I.O. criticized because rural drivers are subsidizing urban drivers.
- M.P.I.C. criticized because older drivers may be subsidizing younger drivers; and “all-purpose” and pleasure drivers subsidizing business drivers.
- I.C.B.C. initially made classification changes which improved the lot of younger drivers and made some territorial changes but public reaction has forced them to withdraw changes to the classification system that result in cross-subsidization.

Hidden subsidies may be utilized to cloud true costs:

- police and medical reports in Saskatchewan.

The government corporation may become a political vehicle and deviate from sound insurance practices:

- I.C.B.C. commitment that no driver would pay more under Autoplan than under private industry resulted in refunds in the first year to certain classes of drivers.
- application of the gas tax is subject to political policy.

Operational start-up problems and costs:

- I.C.B.C. problems with short implementation stage, aggravated by withdrawal of private insurers.

Vulnerability to labour problems and pressure groups, i.e. body shop operators and tow truck fleet operators:

- I.C.B.C. problems with strike.
- S.G.I.O. strike apparent in early 1978; March 1978 settlement reached without disruptions.

Problem of control over monopoly prices:

- a public board or similar mechanism may be required to approve price changes, if accountability through the political process fails to work.

No freedom of choice or comparison for consumer on basic coverage.

Tendency to oversimplify adjusting decisions:

- Saskatchewan consumer annoyance at the frequency of 50-50 fault decisions resulting in loss of deductible and accident surcharge.
- M.P.I.C. and I.C.B.C. adjusting experience does not appear to demonstrate this tendency.

Not necessarily a solution to problems with the products offered:

- consumer unaware of his coverage.
- difficulties with consumer education.

3. Further Considerations

It is impossible to weight the apparent advantages and disadvantages of government ownership in a manner which will provide a factual or statistically supportable answer to the government versus private ownership question. The entire topic is a matter of judgement and opinion which is laden with philosophical, economic and social issues on which different observers will place different emphasis.

A government insurance corporation is normally offered as the extreme solution to a greater government intervention in the automobile insurance industry. Nevertheless, it is apparent that government ownership can serve as an effective vehicle for introducing significant improvements into the insurance system. In general, some of the major benefits include:

- Government ownership is an effective solution to the problems of availability and compliance with a requirement for compulsory insurance coverage.
- Government ownership encompasses a one-company system of operation which appears to provide some measure of savings to the consumer of automobile insurance. These savings can either be used to contain premium costs or to increase the benefits from the insurance pool.
- A government corporation is expected to be directly responsible and accountable to the public in the Province. Its mandate is to administer insurance funds in the economic and social interests of the community it serves.

There is, however, a further dimension to the question of government ownership in the Province of Ontario, which is demonstrated in part by the following considerations:

- It is apparent that, while a government corporation may be a credible solution to some problems, it will create a number of new ones, and may be incompatible with the free enterprise philosophy accepted and practised by the business community and by a large segment of the public in this Province.
- Government ownership of automobile insurance in Ontario would pose a significant implementation task. Government administration of bodily injury alone would compare in size with the operation of I.C.B.C. Inclusion of property damage would demand a much greater financial and organizational requirement.
- Government ownership of automobile insurance in Ontario might have far-reaching consequences related to the following facts:

1. Automobile insurance in Ontario accounts for 44%¹ of the total Can-

1. Annual Report, Federal Superintendent of Insurance, Business of 1976, Table XIV.

ada-wide automobile insurance business of private companies in Canada.

2. With Quebec bodily injury coverage eliminated from the private market, it is estimated that automobile insurance in Ontario will account for about 50%¹ of the total Canadian business of private insurers.

The above facts demonstrate that Ontario is the dominant automobile insurance market in Canada under the private sector. As a result, exclusion of private industry from all or a major share of the Ontario market could have serious consequences in other Provinces of Canada: it could precipitate industry withdrawal from the remaining half of the Canadian private automobile insurance market.

- The potential impact of government ownership of automobile insurance on other general insurance lines must also be taken into account, based on the following facts:

1. Automobile insurance in Ontario accounts for 45%¹ of the total general (other-than-life) insurance business in this Province.
2. The general insurance industry in Ontario accounts for 37%¹ of the general business (excluding automobile) of private companies in Canada.

If automobile insurance were made public, a number of general insurance carriers, who rely on automobile insurance for a major portion of their business, might withdraw entirely from the Ontario market—resulting in a serious shortfall of capacity in the general insurance lines. A government corporation might then be required to take on some share of general insurance, adding to the already considerable task of implementation in automobile insurance. Furthermore, company withdrawal in Ontario might extend to withdrawal from general insurance lines in other Provinces.

- The economic effect of government ownership on the livelihood of insurance company employees, and on agents, brokers, adjusters and their employees must also be taken into account. The importance of this consideration is demonstrated by the following facts:

1. The private general insurance industry in Ontario employs an estimated 16,300 company employees in 236 companies.²
2. The general insurance industry uses the services of approximately 1,350 adjusters, and an estimated 12,000 agents, brokers and their employees.²

Government ownership of automobile insurance would affect at least half of the close to 30,000 general insurance industry employees in this

1. Annual Report, Federal Superintendent of Insurance, Business of 1976, Table XIV.

2. Insurance Bureau of Canada, *Facts of the General Insurance Industry in Canada*, 5th Edition, July 1977.

Province. It is evident that the provincial corporation would absorb a segment of private industry employment, but a significant restructuring of job opportunities is likely to result. Should a provincial corporation be required to take on some share of general insurance in other than the automobile lines, the impact on the industry employment structure would widen.

The above factors cannot be ignored in the eventual resolution of the government versus private ownership question in this Province. However, the enormity of the problems suggested need not preclude consideration of the benefits normally attributable to government ownership. Rather the advantages and disadvantages of government ownership might be separated from the size of the task and its probable industry consequences.

In so doing, it is possible to deal with the question of a government auto insurance corporation on its own merits. Accordingly, it is possible to comment on those elements of the marketing, administration and claims adjusting structure of government ownership which might be worthy of "emulation" by private industry—to the extent that such elements are identified. In addition, government ownership could be considered as one of the several solutions available for government regulation of the insurance industry; or as a necessary solution, if private industry fails to demonstrate at some point in time that it is serving the motoring public efficiently and effectively.

As a further consideration, it is possible to comment on the desirability from the consumer point of view of particular forms of partial government ownership, for example:

- bodily injury coverage only.
- liability coverage and Accident Benefits coverage only with all forms of own-vehicle coverage left to the private sector.

Given conclusions on the above matters, the final decision on government ownership cannot be made without a detailed feasibility study of the costs of industry reorganization to a single, government-controlled corporation or forms thereof. Included in the costs must be the consequences of possible industry withdrawal from other insurance lines.

APPENDICES

- APPENDIX A Underwriting and Rating
- APPENDIX B Marketing and Delivery System
- APPENDIX C Descriptions of Claims Handling and Settlement
- APPENDIX D Adjustments to S.G.I.O. Results

APPENDIX A Underwriting and Rating

SASKATCHEWAN

a) Sources of Premium Income

Premiums earned under the Automobile Accident Insurance Act of Saskatchewan include the proceeds from four separate income sources:

1. *The Certificate of Insurance Premium*

Private vehicle premium rates are based on the *make* and *model* of the vehicle, classified under 12 rate categories. These rate categories combined with the *model year* of the vehicle designate the premiums to be charged. Prior to 1976, the private passenger vehicle class was rated according to year and wheelbase, but the more equitable factor of the value of the vehicle (based on model and size of vehicle) has been substituted.

1977 passenger vehicles premiums vary from \$24 to \$276 for basic coverage that includes Accident Benefits, third-party liability of \$35,000, and a \$200 deductible comprehensive coverage.

2. *The Drivers' Licence Fee*

The drivers' licence fee is determined by the number of rating units accumulated by the driver over a 36-month period prior to the date of application. Conviction under the Vehicles Act, Municipal by-laws, Criminal Code of Canada or similar conviction are assigned a certain number of rating units.

This fee is payable at the time of driver licence renewal. The basic fee in 1977, with 3 or less rating units, was \$5.00. 22 or more rating points are assessed a premium of \$170.00, plus \$10.00 for each additional unit over 21.

In order to encourage more responsible driving, the rating units system incorporates an accelerated earnback for those persons showing improvement in their driving habits. If it is established that no convictions were entered on the insured's driving record during the licence period

immediately preceding the period in which he is applying, a reduction is made of the rating units in the earlier period of one-half of the accumulated rating units on the driver record.

There is no appeal from increases in the basic fee resulting from the accumulation of rating units for traffic convictions and suspensions as these matters have already been decided in a court of competent jurisdiction.

3. *The Motive Fuel Tax*

Effective in 1974, a 3 cent per gallon tax on motor vehicle fuel has been designated as an insurance premium under the A.A.I.A. and is collected by the Department of Finance, Taxation Branch.

4. *Investment Income*

Interest income from investments made with surplus and reserve funds in the A.A.I.A. Fund is taken into account in calculating future premium requirements. The total investment of S.G.I.O. (including A.A.I.A. and other business lines) amounted to \$77 million at December 31, 1976. A major portion of these investments is in the form of Saskatchewan securities. 1976 investment income allocated to A.A.I.A. was \$6.1 million.

An approximate distribution of income collected under the Automobile Accident Insurance Act is as follows:

	1976 Income	Percent
Certificate of Insurance Premium*)	\$57,500,000	77%
Drivers' Licence Fee)		
Motive Fuel Tax	11,000,000	15
Investment Income	6,100,000	8
	<hr/> \$74,600,000	<hr/> 100%

* Basic Coverage only

b) **Rating for Basic Coverage**

The Saskatchewan motorist is charged for compulsory insurance coverage based on simple facts, such as the use of the vehicle (fuel tax and basic drivers' licence fee); value of the vehicle (determined by year, make and model categories); and the driver record (rating point surcharges) to encourage more responsible driving.

Rate categories determined by "risk" classification of the vehicle owner are not utilized by underwriters of *basic* coverage in Saskatchewan. That is, age, sex, marital status or occupation, which are used by most private insurers to determine the likelihood of an accident, have no bearing on premium rates for basic coverage in Saskatchewan. Likewise there is no driver experience or territorial rating.

c) Extension Coverage

The S.G.I.O. also offers, on an optional basis, a package policy which extends the motorist's coverage by the following limits:

- a) Third-party liability and passenger hazard coverage, with a \$200,000 inclusive limit or higher.
- b) Reduction of the \$200 deductible on collision, upset, and plate glass to \$25, \$50, or \$100.
- c) Elimination of the \$200 deductible on all other of the comprehensive coverages (fire and theft, etc.).

Premiums for the Automobile Package Policy are based on the following rate categories:

- City or Rural Driver;
- Accident record in past three years;
- Driver and vehicle use characteristics, including:
 - under or over 25 years of age;
 - sex, marital status;
 - business or pleasure use;
 - private passenger or fleet use;
 - driver training credit.

Although the cost of the total extension Automobile Package Policy is only about one-third of the cost of compulsory coverage, a much more complex system of rating is used to determine premium rates.

d) Other Premium Charges

Under the Saskatchewan rating system, the poor or accident-prone driver is penalized by a \$25 surcharge applied to the certificate of insurance premium if he is 50 percent or more responsible for an accident which results in a claim payment under A.A.I.A. of \$100 or more in the preceding calendar year. Drivers assessed an accident surcharge may appeal by way of the Small Claims Enforcement Act. Only one surcharge per licence year is applicable.

The Act also provides for a rate adjustment in the form of an additional premium, if the S.G.I.O. finds that a driver has misrepresented his accident or offence record, or if the S.G.I.O. considers the owner or operator to be "disproportionately hazardous to himself or to the public". This permits the S.G.I.O. to manually review bad risks on an individual basis. Any additional rates charged are subject to the review of a Rates Appeal Board. Similar provisions are in force in Manitoba and in British Columbia.

e) Fleet Operations and Commercial Vehicles

Commercial vehicles are assessed a premium according to schedules set out under Regulations to the A.A.I.A. In addition, fleet operations are

monitored manually. Underwriters review claim files yearly together with premium income. If an unacceptable loss ratio results, then additional premiums are assessed on a manual basis. The fleet operator is forwarded a notice or appeal together with his notice of assessment and is able to present his appeal before a member of the Rates Appeal Board.

MANITOBA

a) Sources of Premium Income

Premiums earned under the Manitoba Public Insurance Corporation Act include proceeds from four separate income sources:

1. Vehicle Insurance Premium

Passenger vehicle premium rates are based on the following rating factors:

- model year;
- vehicle make/model;
- vehicle body style;
- number of engine cylinders.

These factors define a rating group. The Autopac premium is then determined according to the following characteristics:

- 10 vehicle rating groups;
- 4 classes of vehicle use (preferred, all purpose, farmer and business);
- 4 rating territories.

These same factors are used to determine premium levels for both compulsory basic coverage and optional extension coverage.

The vehicle insurance premium is payable at the time of vehicle registration. The premium cost of basic coverage, including Accident Benefits protection, minimum liability coverage and a \$200 deductible all perils coverage, varies from \$40 to \$199. Extension of liability limits from the compulsory \$50,000 limit to \$100,000 costs on average an extra \$8.00.

2. Drivers' Licence Fee

In addition to the basic \$3.00 drivers' licence renewal fee, Manitoba motorists are charged a basic driver insurance premium according to the following table:

Age	Male	Female
16-24	\$30	\$15
25-64	\$15	\$10

Secondly, a further premium assessment is made based on demerit points. Six demerit points result in a \$100.00 additional fee; while 20 or more demerit points result in a \$350.00 insurance fee.

3. Gasoline Tax

Since May 1975, a 2 cent per gallon gasoline tax has been designated as revenue under the M.P.I.C. Act.

4. Investment Income

Interest income from investment is taken into account in calculating future premium requirements.

At October 31, 1976, \$27,000,000 of M.P.I.C. automobile insurance funds were invested in long-term debentures including the Manitoba Telephone System and the Manitoba Hospital Commission.

An approximate distribution of income collected under the Manitoba Public Insurance Corporation Act is as follows:

	1976 Income	Percent
Vehicle Premiums Earned*	\$72,300,000	77%
Drivers' Licence Fees Earned	10,600,000	11
Gasoline Tax	6,500,000	7
Investment Income	4,500,000	5
	<hr/>	<hr/>
	\$93,900,000	100%

* Basic and Extension Coverage

b) Rating

As in Saskatchewan, Manitoba's motorist is charged for insurance coverage based on simple facts such as his use of the automobile (gas tax and basic drivers' licence fee); the value of his vehicle (based on 10 vehicle rating groups); and on the driver record (demerit point surcharges). Manitoba also takes into account four classes of vehicle use and four territorial classes in order to account for some classification of risk.

Saskatchewan accounts for high risk and low risk use only for its extension coverage; Manitoba incorporates identical, but limited risk factors in rating for both compulsory and extension coverages. Manitoba does not account for factors such as age, sex or marital status in its calculation of premium rates.

c) Other Premium Charges

Manitoba, in concert with British Columbia and Saskatchewan, applies driver premium surcharges based on a demerit point system. As these surcharges are applied at the time of driver licence renewal they apply to all

drivers and not just to vehicle owners as under the private industry system of surcharging.

Furthermore, an accident surcharge is applied in accidents for which the driver has been found 50% or more responsible. Two accidents in twelve months call for a \$50.00 surcharge and each subsequent accident in the same period calls for a \$100.00 additional charge.

An additional premium may also be assessed against a person who has withheld information concerning his accident or convictions record, or who is assessed to be disproportionately hazardous to himself or to the public. An appeal of the additional premium or of accident surcharges may be filed with a member of the Rates Appeal Board, who has the power to confirm, vary or rescind the additional charges.

d) Fleet Operations and Commercial Vehicles

Fleet and commercial vehicle operators pay a basic book premium at the beginning of the year as set out in the Regulations to the Automobile Insurance Act. Based on actual experience over the year, surcharges or rebates become applicable at year end. A "stop loss" provision limits the size of any one claim that is added to annual loss experience.

BRITISH COLUMBIA

a) Sources of Premium Income

Premiums earned under the Automobile Insurance Act of British Columbia include the proceeds from three separate income sources:

1. The Vehicle Premium

The cost of the insurance certificate premium is based on a rating system which calculates the likelihood of the driver being involved in an accident. The rating factors used for private passenger vehicles and light commercial vehicles are:

- marital status;
- age and sex of the driver;
- how the vehicle is used—business or pleasure;
- territory in which the vehicle is primarily used;
- value and size of the vehicle, based on make, model and year.

The first three vehicle-use factors determine 8 rate categories, which are then matched with 14 vehicle rating groups and six territorial codes to determine the relevant premium rate.

These same factors are used to determine premium rates for both basic and extension coverage.

The premium cost of basic coverage for the preferred use class 01 varies from \$99 to \$137. This premium relates only to Accident Benefits coverage and the \$75,000 minimum liability coverage. Extension of liability limits from \$75,000 to \$100,000 costs about \$4.00 on average.

Basic coverage in British Columbia does not include own vehicle damage insurance. Cost of collision damage insurance depends on the extension option selected. Rating factors used to establish premiums include the year, model and make of the vehicle combined into 12 vehicle rating groups, plus the territory of use. The minimum cost of a \$200 deductible collision coverage was \$60 in 1977.

2. *The Drivers' Licence Fee*

The drivers' licence fee is payable at the time of driver licence renewal. The premium rate is determined based on the number of point penalties recorded for the preceding three years on the applicant's driving record. Three points per year are deducted from the total of offences recorded during the first two of the three years counted.

Drivers with a total of 6 or more demerit points are billed annually an amount equal to the square of the net 3-year demerit point total. The minimum charge is nil for no demerit points, up to \$400 for 20 or more demerit points.

3. *Investment Income*

Interest income earned by I.C.B.C. is taken into account in calculating future premium requirements.

An approximate distribution of income collected under the Automobile Insurance Act Fund is as follows:

	1976/77 Income	Percent
Vehicle Premiums Earned*	\$347,300,000	90%
Drivers' Licence Fees	7,500,000	2
Investment Income	30,200,000	8
	<hr/> \$385,000,000	<hr/> 100%

* Basic and Extension Coverage

In 1975, drivers' licence fees amounted to \$14,300,000 or 8% of revenue. A substantial decrease in accident frequency in the 1976 premium year resulted in a decrease in penalty premiums charged. No fee is payable if a driver's record is clear.

Legislation in British Columbia provides for the Corporation to receive from the Consolidated Revenue Fund (Section 16.2) a gasoline tax amounting to 10 cents per gallon. This Section of the Act has not been utilized.

b) Rating

A simplified rating structure was originally applied when the Insurance Corporation of British Columbia was first established. The original rating scheme was based on two categories of vehicle and three vehicle rating factors: market value, 6 territorial areas; and 4 use classifications. These factors were similar to those currently in use in Manitoba.

However, a standard rate structure that did not take into account driver characteristics resulted in substantial cross-subsidization of risk classes. This method of rating was found to be unacceptable to the British Columbia motoring public. As a result, the rate classification system was expanded to include a more traditional range of rating factors: likelihood of an accident, based on vehicle use and driver characteristics; repair costs of the vehicle, based on value and size of the vehicle; and driver record, based on demerit points. The rating system now used by I.C.B.C. takes into account risk factors which are not utilized by the government insurers in Manitoba and Saskatchewan.

Further expansion of rate classes to a more detailed classification system is proposed. For example, I.C.B.C. is planning to break up the young driver classification into smaller units, and to accumulate separate loss experience for these smaller classes. Differentiation in premiums based on 2-year age intervals is planned for the under 25 age group.

c) Other Premium Charges or Discounts

As in the other two government ownership Provinces, I.C.B.C. is able to assess an additional premium if it determines that the driver of a motor vehicle is disproportionately hazardous compared to overall accident experience of drivers in the same rate class or subclass. This assessment is subject to appeal to the Rates Appeal Board established under the Act.

I.C.B.C. does not impose any further accident surcharges, but it has initiated three discount programmes which apply to the insurance premium:

1. A 25 percent discount, on basic premium only, is paid as a "handicapped" discount, and as a "senior citizen qualifying as a pleasure driver" discount.
2. A "safe driving discount" equal to 17.5 percent was applied in 1977 to the amount of the basic and extension insurance premiums combined. To qualify for this discount, the vehicle owner must be claim free over a 12 month period, or at least not be responsible for any claim submitted with respect to his vehicle.
3. A "single male under age 25 safe-driving incentive grant" equal to 25 percent of the amount of basic and extension coverage insurance combined. The under 25 driver must be free of claims for which he had any

degree of responsibility and may not have more than 5 penalty points accumulated on his driving record over the previous year.

The 17.5 percent Safe Driving Discount was introduced in 1977 primarily as a measure to distribute a portion of the surplus in the A.I.A. Fund and resulted in a reduction of approximately \$52 million in 1977/78 premiums. Similarly the Under 25 Safe Driving Discount has been employed to redistribute excess premiums and may be discontinued when a new set of under 25 rate classes is put into effect.

In 1978, the discount programme was amended as follows: a 15 percent discount is now applied if a driver has a one year claim-free record and a 25 percent discount is available to the driver with a two year claim-free record. The Safe Driving Incentive Grant for single males under 25 will remain for 1978, providing a 25 percent discount. About \$6 million was distributed under this programme in 1977.

I.C.B.C. estimates that some ninety percent of vehicle owners in the Province have established one or two year safe driving records. No-fault Accident Benefits claims do not affect safe driving records.

d) Fleet Operations and Commercial Vehicles

Light commercial vehicles are rated according to similar characteristics as the passenger vehicle. Special risks, such as dump trucks or industrial machines are assigned a separate rate class and are rated according to value and use.

Commercial vehicles falling under fleet operations are included in a special Fleet Plan that permits the fleet operator to earn a substantial credit at the end of the loss year. Rebates are assessed on the basis of annual loss experience of individual fleet operators. A similar plan for garage fleets is available.

APPENDIX B

Marketing and Delivery System

SASKATCHEWAN

a) The Insurance Product and the Marketing System

Basic insurance coverage in Saskatchewan is tied to the licence plate and is purchased at the time of vehicle registration. Evidence of basic insurance is provided by a Vehicle Insurance Certificate. Motorists do not receive a copy of the policy. As information regarding the coverage under the basic policy, Saskatchewan issues an annual "Auto Insurance Guide" which explains details of coverage and the basis for premium assessment. This guide is available on demand.

Elimination of the policy form results in savings to S.G.I.O. as it is not required to print, file, endorse or retrieve policy forms. However, most motorists in Saskatchewan are said to be unaware of the provisions under their basic coverage, and often seek advice from agents who sell them extension coverage, rather than make use of the "Red Auto Guide". There is no other continuing education programme to better inform them.

Compulsory first-tier coverage is sold through the following channels:

- directly through 7 motor vehicle registration branches across the Province;
- by 425 licenced issuers of motor vehicle registrations.

Saskatchewan requires that all extension coverage be provided under a separate policy. Again, S.G.I.O. issues only a certificate to indicate proof of extension coverage under its "Package Policy". A separate booklet is available on demand outlining the "insuring agreements". S.G.I.O. extension coverage is not available through the motor vehicle licencing system, but is sold by about 530 independent agents who also sell general insurance and the auto extension policies of private insurers. For the most part, these agents do not sell compulsory first-tier coverage unless they are also licenced issuers of motor vehicle registrations (only about 25 percent have both roles). This system separates sale of compulsory and extension coverage and thereby permits private insurers to remain in competition with S.G.I.O. for automobile extension policies.

Close to 700,000 automobiles are covered by S.G.I.O. basic coverage, while 200,000 drivers have purchased extension policies from S.G.I.O. It is estimated that S.G.I.O. policies represent 70-75% of the market for extension automobile coverage.

b) The Licencing and Insurance Renewal System

On April 1, 1977, the Saskatchewan Government Insurance Office undertook operation of the motor vehicle licencing system on behalf of the Motor Vehicle Board. The Motor Vehicle Division of S.G.I.O. appoints all licence issuers, who are also responsible for the issuance of the compulsory insurance certificates. The Motor Vehicle Division also maintains a driver file of convictions and infractions.

Saskatchewan presently operates under a staggered system of registration renewal. Owners were offered a voluntary choice of the renewal date, and are assessed their insurance premium for compulsory coverage on this date as well as being required to re-register their vehicles. Licence plates have a sticker indicating the month of expiry of the registration and insurance certificate.

Driver licences are now renewed according to the birth month of each driver. Prior to May 1977, renewals fell on the common date of May 1st.

c) Selling Costs

Commissions (known as processing fees) for compulsory first-tier coverage are paid by S.G.I.O. on a flat-rate per transaction basis of \$1.50 for each insurance transaction and \$1.00 for each licence plate renewal. These commissions are paid only to licenced issuers of insurance certificates; motor vehicle registration branches are not paid any fee for handling direct purchases of tier-one coverage.

Agents selling S.G.I.O. extension coverage are paid a commission of 17.5%. As the agents selling extension coverage are generally not exclusive to S.G.I.O., their commission rates reflect a level of selling costs associated with a similar package of coverage provided by competing private insurers.

For basic and extension coverage combined, the average selling cost is 3½-4½% of the premium value.

d) Financing Plan for Compulsory Coverage

S.G.I.O. provides no financing plan for purchase of compulsory basic coverage. The full premium is payable at the time of vehicle re-registration. Because government automobile insurance has been a "way of life" for many years in the Province, the public appears to accept this requirement virtually without question.

e) Role of the Agent

The agent in Saskatchewan functions primarily in the general insurance lines. Although automobile extension policies are generally unavailable through the motor vehicle licencing system, thereby making them the exclu-

sive domain of the agent, agents sell automobile extension policies mainly as a service to clients who buy other forms of insurance.

Despite a relatively high commission rate, premiums average about \$40-\$50, such that fees normally fall below \$10 per transaction. The fee per transaction will become even less attractive to the Saskatchewan agent should S.G.I.O. decide to expand first-tier compulsory coverage. This action would have the effect of reducing the premium value of extension policies bought by Saskatchewan residents.

f) Role of Private Insurers

Private insurance companies compete with S.G.I.O. for automobile extension policies, either directly through their own sales-people or through independent agents. However, the private insurance company finds it difficult to make a profit on automobile insurance coverage sold on its own. Premiums must be kept low to compete with S.G.I.O., however the expenses incurred are high. The private insurer is unable to take advantage of savings available to S.G.I.O., such as the same adjuster handling both basic and extension policy claims.

As a result, private companies hold only about 25-30% of the automobile extension insurance market and are continually losing in share to S.G.I.O. As in the case of the agent, any expansion of compulsory coverage by S.G.I.O. will further reduce the attractiveness of the automobile insurance market to private industry.

MANITOBA

a) The Insurance Product and the Marketing System

Manitoba provides both basic coverage and extension coverage, other than special risks, under one vehicle registration and insurance certificate document. As in Saskatchewan, a Vehicle Insurance Certificate is provided as the only proof of insurance. A separate booklet is published outlining basic coverage and extension options available from Autopac. This booklet is available on demand at all Autopac outlets. Motorists do not receive a copy of the automobile insurance policy; instead they presumably receive the benefits normally associated with lower production costs.

Compulsory first-tier coverage and extension coverage are sold together, if extension coverage is chosen, through the following channels:

- directly by mail or through Autopac offices;
- by Motor Vehicle licencing branches;
- by independent agents, who sell both automobile and other general insurance policies. Agents who sell Autopac policies are also licenced to issue motor vehicle registrations.

Approximately 85% of M.P.I.C. automobile policies are written by

Autopac agents; only 15% are sold directly by or through motor vehicle licencing branches.

b) The Licencing and Insurance Renewal System

On April 1, 1973, the Manitoba Public Insurance Corporation assumed responsibility for administration of the motor vehicle licencing system. As a result, M.P.I.C. licences its Autopac agents to issue both motor vehicle registrations and insurance coverage.

Manitoba operates under an annual renewal system for motor vehicle registration and renewal of insurance coverage. The deadline date is February 28. Approximately 500,000 documents are processed in six weeks of each registration year. Driver premiums are assessed annually on the birth-date of the driver.

c) Selling Costs

Commissions for Autopac policies are allocated as follows:

- There is no transaction fee paid on direct purchases of insurance from Autopac outlets or Motor Vehicle branches.
- Agents selling basic coverage are paid 5% of the premium (7% in 1972 and 6% in 1973).
- Commissions on optional extension coverage (excluding special risks) are paid at 10% of the premium value.
- Commissions on special risks, such as fleets, motorcycles or commercial vehicles, are paid within a range of 7.5% to 12% on the value of the premium.

In addition, agents also handle motor vehicle registration transactions and are paid administrative fees of \$1.20 per validation transaction.

Agents are post-paid monthly by Autopac for transactions processed due to insurance premiums. Where an instalment payment is indicated, commissions are still calculated on the total insurance premiums assessed.

Agents' commissions average about 4-6%, a little below average commissions paid in British Columbia. Extension coverage policies carry a 10% commission rate which is considered by M.P.I.C. to be equitable given that extension coverage is purchased in conjunction with renewal of basic coverage, and requires little additional selling effort by the agent.

d) Financing Plan

Total fees must be collected by agents at the time of application for all transactions except new applications and renewals. There is an instalment payment plan available for renewals and new applications for the following registration classes: passenger car, delivery car, truck and farm truck.

The instalment plan consists of two payments. The first instalment is payable at the time of application, and the second instalment is payable 90 days after the commencement of the new registration year or the effective date of the transaction. A flat "time payment administration fee" of \$3.00 is charged for this service which approximately 100,000 motorists took advantage of in 1976 out of a vehicle population of about 500,000.

e) The Role of the Agent

The agent is an essential part of the marketing mechanism for Autopac policies. Similarly, the agent relies greatly on the transaction of business for the M.P.I.C., as private industry presence in auto insurance in Manitoba is small.

The agent in Manitoba sells both compulsory and extension coverage on the same insurance certificate. Unlike Saskatchewan, where an increase in compulsory coverage limits could severely curtail the role of the agent who sells only extension policies, Manitoba's system safeguards the function of the agent.

Although Autopac agents receive a fee which is lower than the normal private industry commission fee structure, agents are considered to be better off under Autopac than under the private system for the following reasons:

- They are no longer required to deal with policies and no longer incur high mailing charges.
- They no longer have any accounts receivable or bad debt problems.
- There are no chargebacks on commissions for cancellations, etc.
- They are paid a processing fee for policy changes.

Unlike the other two government ownership Provinces, agents in Manitoba who "qualified" by earning at least 25% or \$2,000 of their gross income from automobile insurance commissions, were offered some transitional assistance in the form of cash assistance or loan guarantees, to ease the transition from a private market for automobile insurance to a largely government-controlled market. Cash assistance grants totalling approximately \$1,200,000 were provided by the Corporation.

f) Role of Private Insurers

Private industry presence in the Manitoba automobile insurance market is currently very small. Most private insurers, since 1974, have withdrawn their facilities in the automobile extension insurance field. As a result, Autopac policies account for some 90% of extension coverage carried by Manitoba motorists.

With the entry of M.P.I.C. in 1975 into the field of general insurance, several companies also withdrew their general lines from the Manitoba mar-

ketplace, but M.P.I.C. has gained only a small share, under 10%, of this market.

BRITISH COLUMBIA

a) The Insurance Product and the Marketing System

British Columbia provides evidence of both basic coverage and extension coverage (other than special policies) under one vehicle registration and insurance endorsement certificate. As in the other two government ownership Provinces, a Vehicle Insurance Certificate is provided as the only proof of insurance. A separate booklet is published annually, summarizing the insurance policy, and providing information on claims reporting. No policy form is printed. The actual "policy" is made up of the Automobile Insurance Act and Regulations pursuant to the Act.

Compulsory first-tier coverage and extension coverage are sold together, if extension coverage is chosen, through the following channels:

- directly by mail or through Autoplan offices;
- by 116 motor vehicle licencing branches, which account for roughly 15% of Autoplan transactions;
- by 780 independent agents, which account for approximately 85% of Autoplan transactions.

Both the motor vehicle branch and the agents are authorized to issue the registration renewal (licence plate) and the insurance certificate.

b) The Licencing and Insurance Renewal Systems

Unlike Saskatchewan and Manitoba, the Motor Vehicle Licencing system in British Columbia is operated separately by the Motor Vehicle Branch. Nevertheless, I.C.B.C. makes use of M.V.B. facilities for a small proportion of its insurance transactions, whereas the M.V.B. makes use of Autoplan agents for a large proportion of its registration transactions. Autoplan agents handle routine licence renewals, transfers of ownership and other designated changes or corrections. More complex licencing transactions must be performed by the Motor Vehicle Branch.

Renewal Insurance Certificates and Licence Certificates are forwarded by I.C.B.C. to the vehicle owners in the Province annually in December, and the certificate must be validated by February 28th of the year following. The certificates are reasonably simple to complete and are validated by a stamp. At the time of validation, the motorist selects the extension coverage he wishes over basic insurance, and evidence of the extension insurance forms part of the original Insurance Certificate.

At the same time a licence plate decal is issued which is attached by the motorist to the metal plate on his vehicle. The insurance coverage and the licence become effective March 1st annually.

A system of staggered renewals based on the birth-date of the vehicle owner is planned, but its implementation in 1977 was postponed due to operational difficulties. At the present time, 2-2½ million registration and insurance certificates are processed each year between December and March.

Drivers' licence fees and surcharges are assessed separately and billed annually on the birth-date of the driver. Non payment results in non-renewal of the driving licence.

c) Selling Costs

Agents' fees or commissions for automobile insurance for the 1977 motor vehicle licence year are as follows:

- The fee payable for each new or renewed certificate of insurance submitted to the corporation is \$3.50.
- The fee payable for each mid-term endorsement is \$3.00.
- The commission payable for extension insurance or other non-compulsory automobile insurance is 10 percent of the premium paid for such insurance after allowance of any applicable discount.
- In addition to the above fees payable, a performance bonus commission of \$1.50 may be paid to an insurance agent for each new or renewed certificate and mid-term endorsement that does not include any error in the information set out so that the information is acceptable by the corporation data processing system.

The commission payable on the basic automobile insurance premium has been reduced from 9% in 1974, 7% in 1975 and 5% in 1976 to a \$5.00 total flat rate per policy in 1977.

The flat rate commission for basic coverage is considered preferable because under the percent commission system agents were earning higher fees for handling higher risk drivers without any commensurate difference in amount of work.

The \$5.00 flat rate commission applies to coverage which includes only Accident Benefits and minimum third-party liability insurance. Based on 1977 premiums for basic insurance, the \$5.00 fee amounts to 5% or less of the premium value, depending on risk class.

Vehicle damage coverage, which falls under compulsory insurance in Manitoba and Saskatchewan, is part of extension coverage in British Columbia and is subject to the higher 10% commission rate paid to agents.

The average commission received by the agent in British Columbia in the first six months of 1977 was 7.5%, higher than the 4-6% average in Manitoba and the much lower 3½-4½% average in Saskatchewan (when both compulsory and extension coverages are added to the potential total premium base).

d) Financing Plan

I.C.B.C. provides for a premium instalment financing plan. This plan requires full payment of licence plate fees and a 25% downpayment on the insurance premium for both basic and extension coverage and three instalments payable at two-month intervals. These payments can be charged against the vehicle owner's bank account automatically. The interest rate on the outstanding balance is 15% per annum.

115,000 finance contracts were written in 1976. I.C.B.C. is finding that revenues do not offset bad debts. In addition, collection of bad debts is difficult because it requires the costly process of collecting licence plates before policies are effectively cancelled. I.C.B.C. would prefer to eliminate the plan and require cash payments, but government policy calls for the provision of some type of financing arrangement.

e) Role of the Agent

As in Manitoba, the agent is an essential part of the marketing mechanism for Autoplan policies, and he sells both compulsory and extension coverage. In addition to his function of selling insurance, the agent also handles licencing transactions.

Financial assistance was not offered to agents when I.C.B.C. was implemented. All agents that were licenced to sell automobile insurance and had applied to the Corporation in 1973 were permitted to represent Autoplan. Since that time, appointment of new agents has been only on an exception basis. Annual training seminars are now held to offer instruction on new methods and procedures.

f) Role of Private Insurers

Private insurers in British Columbia play a minimal part in the provision of automobile insurance. Despite the fact that the extension policy market in B.C. is substantially larger than in the other two government ownership Provinces, I.C.B.C. accounts for some 98% of direct premiums written.

A major factor that has limited private industry presence is the fact that collision coverage was sold as part of the compulsory basic coverage provided by I.C.B.C. until mid-1976; consequently the size of the extension market has only recently expanded. Furthermore, the tied selling of Autoplan extension coverage to the issuance of the basic insurance certificate is convenient to the consumer and may discourage him from splitting his transaction by buying from competing sources.

APPENDIX C

Claims Handling And Settlement

SASKATCHEWAN

a) Facilities

Eight Claims Centres were in operation in 1977. There is only one Centre in Regina resulting in frequent criticism of delays experienced in going through the Centre on busier days. A salvage depot is also operated in Regina.

b) Staff

S.G.I.O. employs 416 people in its claims division. Increasing business has resulted in staff increases in 1977 to provide necessary service. The ratio of claims handled (compulsory and extension) to staff is about 290, below the level of 400 claims per staff member in Manitoba and British Columbia.

S.G.I.O. is criticized for the inexperience of many of its adjusters. Technical and supervisory training programmes are considered to be good, but the average length of service is short.

Adjusters and other claims personnel are under union contract with the Office and Professional Employees International Union. The Corporation has in general enjoyed a harmonious relationship with its employees although a threat of strike was raised in early 1978. However, no disruptions in service have resulted.

S.G.I.O. uses the services of independent adjusting firms to assist Corporation staff when events such as major storms strain the facilities of the Corporation.

c) Attitude to Claims Settlement

The Corporation is criticized for a tendency to make 50-50 liability judgements. In such a case, both parties lose their deductibles and are often assessed an accident surcharge if the loss is over \$100. This principle of a set-off is financially advantageous to S.G.I.O. but unpopular to drivers.

S.G.I.O. tends to settle at book value rather than at actual cash value, to the disadvantage of the owner.

d) Method of Handling Claims

S.G.I.O. has recently upgraded its claims system for automobile damage claims but remains behind the other two government ownership Provinces in the use of data processing systems for claims handling.

e) Planned Improvements

Revision and modernization of the data processing system is planned.

MANITOBA

a) Facilities

The M.P.I.C. operates 14 Claims Centres or offices, 6 of them in Winnipeg. A separate salvage and commercial claims handling facility is located in Winnipeg.

b) Staff

M.P.I.C. employs in its claims division a total of about 450 people, or 60% of the total corporate staff. Employees are represented by the Manitoba Government Employees' Association. Close to 400 claims per staff member were handled in 1975/76, comparable to the level in British Columbia.

c) Attitude to Claims Settlement

A study of 231,757 claims over a 20 month period indicated the following division of liability in third-party claims:

Fully responsible	41.0%
50% or more responsible	3.0
Less than 50% responsible	0.5
No responsibility	56.0
	<hr/>
	100.0%

50-50 liability judgements are minimal in number. The attitude of the M.P.I.C. is that it always has to pay a deductible in a 2-vehicle accident, and the liability call just decides to whom it will pay.

The incidence of fraudulent claims is controlled by a Special Investigation Unit.

d) Method of Handling Claims

The M.P.I.C. operates under an automated system of claims processing. Direct access via data communications equipment is provided from the claims centre to a computerized driver licence and automobile registration file. This system permits the quick matching of accident files for all vehicles involved in an accident.

e) Planned Improvements

No major improvements are planned at the present time. Manitoba is ahead of British Columbia in the on-line retrieval of accident and claim information at the Claim Centre.

BRITISH COLUMBIA

a) Facilities

I.C.B.C. operates 17 Claims Centres across the Province, plus 9 branch offices. In addition, 15 resident adjusters are employed in more remote communities. Difficulties and inconvenience were encountered by the public during the first two years of Autoplan due to a shortage of facilities and staff. These short-term problems are being successfully resolved.

b) Staff

The claims department of I.C.B.C. employs 1,000 people or 38% of the total corporate staff. Roughly 370 claims per staff member were handled in 1976/77.

Previous criticism of inexperienced adjusters has largely disappeared. A thorough training programme is conducted for adjusters and appraisers, including work at an I.C.B.C. body shop.

Three grades of adjusters are established with clearly defined limits on the size or type of claims to be handled. Claimants are quickly referred to a senior claims adjuster if their claim merits more experienced attention.

I.C.B.C. employees are unionized under the Office and Technical Employees Union. Failure to negotiate a settlement in 1975 resulted in a 3½ month strike and a backlog of unprocessed claims. Staff relations have remained stable since that time, but I.C.B.C. remains vulnerable to organized "pressure groups".

c) Attitude to Claims Settlement

Adjusters are instructed at the present time to keep claim payout low, but fair and proper. I.C.B.C. maintains a record of complaints and finds that less than 1% of claims result in a "justified" complaint. In addition I.C.B.C. has a programme to reinspect at random claims after repairs to determine if the claimant is satisfied and if the adjuster has made an appropriate settlement.

In paying the deductible on property damage claims I.C.B.C. makes use of a collision assessment chart as a guideline towards apportioning fault.

The high political profile of I.C.B.C. initially created an overgenerous attitude towards claims settlement. Better controls are now exercised on claims. More attention is being paid to reducing the incidence of fraudulent claims, through a Special Investigation Unit.

d) Method of Handling Claims

Claim files are presently maintained on a manual basis in the Claims Centre, but are linked to a centralized computer payment processing facility.

e) Planned Improvements

Liaison with the Motor Vehicle Branch gives I.C.B.C. access to two major computerized record files. A "vehicle file" records all vehicles licenced in the Province, details relative to their insurance protection, accident history and claim information. A "driver file" provides a tandem record of all licenced drivers, their licence classifications, infraction and demerit point records and their basic accident histories. Access to these files directly from the agents' office and from the claims centre is planned. Manitoba currently provides direct access to accident records from the claim centre only.

APPENDIX D

Adjustments To S.G.I.O. (A.A.I.A.) Results To Reflect Extension Coverage Experience

<i>METHOD 1</i>	— As provided by S.G.I.O.	
	— Restated 5 year averages combining the A.A.I.A. and the extension results.	
	Premiums Earned	100.0%
	Claims Incurred	86.9
	*Claims Expenses	8.0
	Commissions etc.	6.5
	Administrative Expenses	7.2
	Total Expenditures	108.6
	Investment Income	8.5
	Loss	(.1)%
	∴ Efficiency = $\frac{86.9}{108.6} = 80.01\%$	

* Would likely be slightly high as extension claims could be adjusted and settled at same time as those on basic coverage.

<i>METHOD 2</i>	— Estimated 1976 Experience:	
	A.A.I.A. Premiums Earned	69.5 million
	Tier II Premiums Earned	12.4
	Total Premiums Earned	81.9 million
	A.A.I.A. Claims Incurred	59.0 million
	Tier II Claims Incurred	8.6
		67.6
	A.A.I.A. Expenses including	
	Claims Expenses	13.4
	Tier II Expenses @ 35% of Tier II	
	Premiums	4.3
	Total Expenditures	\$85.3
	∴ Estimated Efficiency = $\frac{67.6}{85.3} = 79.2\%$	

BACKGROUND STUDY THREE

A Government Presence In Rate Regulation

TABLE OF CONTENTS

	Page
A. INTRODUCTION	479
B. THE HISTORY OF RATE REGULATION OF THE INSURANCE INDUSTRY	480
1. In Canada	480
The Federal Superintendent.....	480
The Provincial Superintendent	481
Royal Commission on Automobile Insurance Premium Rates—Ontario—1930	481
Royal Commission on Automobile Insurance— British Columbia—1968	482
Royal Commission on Automobile Insurance— Nova Scotia—1973	483
Insurance Study—Ontario—D. H. Carruthers, Q.C. —1973-1975	484
Current Rate Regulation Provisions in the Provinces	458
Ontario Now	486
2. In the United States	487
The Legislation	487
Forms of Compliance	488
Recent Trends.....	490
3. Recapitulation of Canadian Versus United States Experience.....	493
C. OBSERVATIONS ON THE ONTARIO SYSTEM	494
1. Responsibility for Rate Regulation	494
2. Possible Shortcomings of the Present System in Ontario	495
D. COMPETITION AS A POSSIBLE FORM OF REGULATION IN ONTARIO.....	497
E. OTHER FORMS OF GOVERNMENT REGULATION AS POSSIBLE SOLUTIONS FOR ONTARIO	505

APPENDICES

Appendix A: Rate Regulation in Canada

Appendix B: State Rate Regulatory Laws Applicable to Automobile Insurance

- Appendix C: Monitoring Competition: A Means of Regulating the Property and Liability Business—N.A.I.C.—1974
- Appendix D: Sample Legislation
- Appendix E: The Early Warning System—N.A.I.C. Regulatory Tests for Property and Liability Insurers
- Appendix F: The Insurance Act—Sections 365-367 Pertaining to Rate Regulation

BACKGROUND STUDY THREE

A Government Presence In Rate Regulation

A. INTRODUCTION

During its deliberations prior to issuing its First Report, the Committee considered the question of governmental rate regulation. Representatives of the industry and the Superintendent's Office made presentations to the Committee but it was decided to defer detailed consideration of the matter until later. Specifically, in its "Topics for Subsequent Consideration", the Committee stated with respect to government presence in rate setting: "the Committee will consider this topic more fully in the course of its forthcoming sittings. It will identify various systems in use in other Canadian and United States jurisdictions such as rate setting, file and use systems, use and file systems, etc. The Committee will study the merits of each system with a view to making final recommendations on this topic."¹

Some form of legislated rate regulation is established in the field of automobile insurance in most jurisdictions in North America, with the exception of the government ownership Provinces, Prince Edward Island and Ontario in Canada; and Illinois in the United States. This study examines the various concepts and procedures applied in rate regulation under the following headings:

B. The History of Rate Regulation of the Insurance Industry

This section considers the current powers of regulatory departments in Canada and proposals for increased supervision. Following is a brief review of the historical background and the current trends of regulation in the United States.

C. Observations on the Ontario System

This section raises considerations relevant in reviewing the current system of protecting the public interest and in suggesting alternative proposals for rate regulation in the Ontario market place.

D. Competition as a Possible Form of Regulation in Ontario

Criteria used to determine the existence and effectiveness of competition are outlined in this section, followed by consideration of the mechanisms required to monitor competition.

E. Other Forms of Government Regulation as Possible Solutions for Ontario

This section explores alternative methods of rate regulation in the automobile insurance industry, including enactment of unproclaimed sec-

1. The Select Committee on Company Law, *The Insurance Industry—First Report on Automobile Insurance*, Province of Ontario Legislative Assembly, 1977, page 243.

tions in the Ontario Insurance Act, and discusses other aspects of regulation such as protection against insolvencies.

B. THE HISTORY OF REGULATION OF THE INSURANCE INDUSTRY

1. In Canada

The current powers of regulatory departments are considered in this section along with proposals for increased supervision of the automobile insurance industry. This study will deal with only a few of the multitude of writings, reports, and committees which have considered the question of regulation in the insurance and automobile insurance industry.

The Federal Superintendent

The nature and extent of Federal supervision over insurance is concisely outlined in a memorandum on the supervision of insurance, loan, and trust companies in Canada, prepared by the Federal Department of the Superintendent in 1938 for submission to the Royal Commission on Dominion-Provincial Relations as follows:

- "The department considers that it is its main function to see to it that all companies under its supervision are in a position at all times to meet valid claims made upon them by their policyholders and that so far as can be ascertained at any time, they are likely to do so indefinitely. To enable it to perform this function the acts provide for the submission of annual statements in very great detail by all companies to the department; for an annual examination of those statements at the offices of the companies by the department's examiners; for deposit with the Minister by British and foreign companies of security sufficient to cover their liabilities in Canada; and for the necessary remedies in the event of default on the part of any company. The examination involves the verification of assets shown in the statements; the valuation of the contracts to ascertain the amount of the liabilities; the examination of the contracts to see that the powers conferred by the licenses are not exceeded, and this involves the filing of copies of all contracts; and the examination of the charters or other incorporating instruments to see that the corporate powers are not exceeded, and this involves the filing of all incorporating documents with all amendments thereto."¹

While the above was written in 1938, the present duties and responsibilities of the Federal Superintendent of Insurance are essentially the same.

1. *Report Concerning the Business of Automobile Insurance in Canada*. Restrictive Trade Practices Commission, Ottawa 1960, page 35.

The Provincial Superintendents

Provincial insurance legislation related to automobile insurance is contained in the various provincial statutes. Each Province has likewise established an insurance department or branch under a Superintendent of Insurance. Briefly, the Provincial Superintendents, like the Federal Superintendent, are concerned with the licencing and solvency of insurers and also with the requirement of fair and equitable terms in insurance contracts to safeguard the insuring public.

Accordingly, the duties and responsibilities of the Federal Superintendent and the Provincial Superintendents with respect to the solvency of insurers are essentially the same: the former dealing with federally incorporated companies and British and foreign companies operating in Canada, and the latter dealing with provincially licenced or incorporated companies. In some Provinces such as Manitoba, whose insurance department and regulation requirements are quite small, the matter of solvency of provincially incorporated companies is subcontracted to the Federal Superintendent whose staff perform solvency reviews and examinations on companies incorporated in the Province of Manitoba.

Royal Commission on Automobile Insurance Premium Rates—Ontario—1930

Under the chairmanship of the Honourable Mr. Justice Hodgins, this Commission was established to examine the justification for large increases in automobile insurance premiums which had occurred in the late 1920's. During this examination, many matters came to the attention of the Commission which found their way into Mr. Justice Hodgins' report and which are quite relevant to the current situation in Ontario.

Mr. Justice Hodgins felt that with the implementation of compulsory automobile insurance came a requirement for some form of regulation over the suppliers of such insurance. In reaching this conclusion, Mr. Justice Hodgins considered that, "when any compulsory law was passed requiring any class of the people to pay for procuring a particular thing, there ought to be government regulation of the price, or some public standard, and that the price should not be left to be regulated by those who offered it for sale, as in the case of compulsion there was no chance for competition".¹ However, he also recognized the difficulties in such regulation, as "no general fixed premium could be settled for all parties, because of the various coverages, the extent of liability, the different mechanical equipment of the cars, territorial differences and exposures to risk, etc."²

1. Province of Ontario, *Royal Commission on Automobile Insurance Premium Rates*, 1930, page 25.

2. Ibid.

As Commissioner, Mr. Justice Hodgins viewed his enquiry into the reasonableness of the insurance rate increases as his specific mandate, but secondarily felt that he should consider the existing laws in Ontario with reference to rate regulation and supervision of insurance rates generally. In that regard, and as a result of the findings of the Commission, Mr. Justice Hodgins advised the Attorney-General of the Province to "give authority to the Superintendent of Insurance to order, after due notice, and a hearing before him, an adjustment of automobile insurance rates whenever they are found to be excessive, inadequate, unfairly discriminatory, or otherwise unreasonable".¹ These recommendations are contained in Sections 365 to 367 of the Insurance Act but have never been proclaimed.

Royal Commission on Automobile Insurance—British Columbia—1968

This Commission was established to make enquiry into the losses and expenses resulting from motor vehicle accidents in British Columbia. Among other things, it considered whether a variation or a plan of compensation or such a combination should be administered privately, or by or through a governmental department or governmental agency. After extensive deliberations and examinations of the matter, this Commission concluded that because of the multiplicity of other duties of the Superintendent of Insurance of British Columbia, plus the limitation on his staff and their lack of statistical or actuarial experience, it would not be possible for the Superintendent's Department to perform many of the new requirements that the Commission was recommending.

The Commissioners therefore recommended that a three-man Automobile Insurance Board be constituted to establish the maximum rate on the compulsory basic accident policy; keep an actuarial check on the rates charged by insurers; and perform other duties necessary to maintaining a vigilance over premium rates and over the administrative and selling expenses of insurers merchandising coverage in the Province. In addition, the Board was to act as an investigative and appeal mechanism over complaints made to it on the subject of automobile insurance. Board membership was to include a Chairman with university qualifications in statistics, a member with business and organizational experience but no auto insurance or civil service experience, and a nominee of the automobile insurers licenced to transact business in B.C. The Commissioners felt that neither the B.C. Superintendent of Insurance nor the B.C. Superintendent of Motor Vehicles should be members of the Automobile Insurance Board.

The Commissioners recommended that the B.C. Superintendent of Insurance should continue with the licencing of insurers, agents, salesmen and adjusters, and the establishment of the qualifications for licencing. In addition, the Commission felt that the Superintendent should continue to be re-

¹ Province of Ontario, *Royal Commission on Automobile Insurance Premium Rates*. 1930, page 16

sponsible for regularly checking the solvency of the insurers and their maintenance of adequate reserves. They did not feel, however, that the Superintendent should have responsibility for securing from insurers data on premium income, expense costs or loss ratios covering their annual operations, or establishing that premium rates are fair yet adequate. These duties were delegated to the Automobile Insurance Board, which came into existence for a short period of time, first as part of the Public Utilities Board and later as a separate board, and was succeeded in 1973 by the Insurance Corporation of British Columbia.

The Commission felt that the establishment of an Automobile Insurance Board was preferable to a government takeover of the automobile insurance industry as at the date of their report. They felt that this would give the industry an opportunity to participate in the new compulsory coverage which they had recommended and also to function under the new form of regulation. They went on to say that, if industry was disinclined to proceed with these recommendations, then the government of the Province of British Columbia should take over, as the sole supplier, the role of selling of automobile insurance in that Province.

Royal Commission on Automobile Insurance—Nova Scotia—1973

In its recommendations, this Commission saw no compromise between two polar possibilities. One possibility was the continuance of the status quo in Nova Scotia with some modifications which would involve the Province in a more active and extensive role in supervising and regulating the industry. The other possibility placed the automobile insurance industry under the government sector. The Commission chose the first possibility; it concluded that automobile insurance should be left in the private sector but should be subjected to additional government control.

The Commissioners recommended that the Office of the Superintendent of Insurance be the focal point for governmental regulation and that the Superintendent should have a separate department and the rank of Deputy Minister. They also recommended that the Superintendent's Office should concern itself with supervision of insurance companies and insurance activities, regulation of rates, licencing and examination of agents and adjusters, publication of certain statistical and informational material, receiving and resolving of consumer complaints, and the general education of consumers regarding insurance matters. The Commission also recommended the provision of adequate budgets and staff to fulfill these responsibilities.

The existing legislation in the Province required automobile insurance companies to table their rates and any changes in their schedule of rates with the Nova Scotia Board of Commissioners of Public Utilities. The Commission felt, instead, that these activities would be conducted more properly by the Office of the Superintendent of Insurance. However, the Commission's

recommendations with respect to this expanded role for the Superintendent were not implemented, so that the Public Utilities Board continues in its regulatory role.

Insurance Study—Ontario—D. H. Carruthers Q.C.—1973-1975

In 1973, the Superintendent of Insurance for the Province of Ontario appointed D. H. Carruthers Q.C. to study "with specific regard to the public interest, the relations between insurers and those served or benefited by insurance . . . and in consequence to make recommendations . . ."¹

In general terms, Carruthers reported that the other-than-life insurance industry did a satisfactory job of serving the public; however, that some practices flowing from the structure of the industry, which is inflexible because of the regulatory system, worked against the public interest. The main difficulties were summarized as follows:

- "1. In the buying and selling process and in the claims settlement process, it is not clear to the insured whose interests the intermediaries represent.
2. Inadequate information on costs and benefits is available to the consumer. The problem includes understandability of contracts, identification of hazards included and excluded and expected benefits and costs.
3. The claims settlement process is hard for the consumer to predict and unnecessarily frustrating for many claimants."²

Carruthers described a range of other problems faced by the consumer, many as consequences of the above, and outlined their overlapping nature which rendered solutions difficult.

He concurred with others who suggested that there may be limited competition and efficiency in the areas of selling costs and new product development, and generally concluded that changes should be made to the regulatory system to encourage more efficiency in distribution and in the development of new products which would likely result in cost reductions or service improvements.

He then recommended a revised regulatory system which, among other things, envisaged greater disclosure of costs and benefits by the insurers, consumer access to unbiased and expert advisors to assist with the interpretation of this new information, and development of a wide variety of marketing and distribution techniques. His recommended model embodied the concept of self-regulation by the industry. Coincident with industry self regulation, the Department of Insurance would be entrusted with an evalua-

1. D. H. Carruthers, Q.C., *Report 1 on Insurance Study*, December 12, 1973, Letter of Appointment.

2. D. H. Carruthers, Q.C., *Report 3 on Insurance Study*, February 19, 1975, page 2.

tion role over the system's effectiveness, with licencing and enforcement responsibility, and with the development of disclosure requirements.

Specifically on the matter of rate (premium) control by government, he felt that such control would be impracticable to implement; rather, "a system which allows consumers to see clearly the price and nature of services offered for ready comparison with competitive offerings should be easier to manage, should provide lower prices for a given service level and should provide a wider variety of service levels".¹ In addition, he felt that most proposals for innovation in automobile insurance could be accepted by his recommended regulatory system.

TABLE 1
Rate Regulation in Canada

Public Automobile Insurance Corporations

- British Columbia
- Saskatchewan
- Manitoba
- Quebec (bodily injury only)

Prior Approval

- * Alberta—60 day deemer clause
- * New Brunswick—60 day deemer clause
- * Newfoundland—60 day deemer clause

File and Use

- * Nova Scotia

Filing Law

- Quebec (property damage and liability insurance)

No Regulation

- Prince Edward Island
- Ontario

* Additional detail provided in Appendix A.

Current Rate Regulation Provisions in the Provinces

The status of current rate regulation provisions in the Provinces in Canada is outlined in Table 1 and in Appendix A. Saskatchewan, Manitoba and British Columbia have government owned automobile insurance plans and accordingly there is no requirement for regulation over the automobile insurance industry. Basic automobile insurance coverage is provided in the compulsory plan which is sold exclusively by the government corporations, and

1. D. H. Carruthers Q.C., *Report 4 on Insurance Study*, July 25, 1975, page 90.

in each of the Provinces the private sector is allowed to compete for extension coverage.

Currently, the Provinces of Ontario and Prince Edward Island do not have any formal legislation with respect to government regulation of automobile insurance rates. The Insurance Act of Ontario contains provisions for a greater regulatory role by the government but these provisions have never been proclaimed as law.

In the Province of Quebec, recent legislation has established government administration of bodily injury coverage but property damage coverage will continue to be merchandised by private industry. The Superintendent is required by the new legislation to analyze the rate manuals which must be submitted by all private insurers within ten days of amendment. Each year the results of this analysis must be reported to the Minister, but it is unclear what specific role, if any, the government may have in requiring rate changes.

As can be seen in Appendix A, New Brunswick, Nova Scotia, and Newfoundland currently have various rate regulatory laws which are administered by provincial public utilities commissions. In Alberta on the other hand, an automobile insurance board was established in 1971 to regulate rates and monitor the industry.

The Committee's discussions with members of I.B.C. have indicated that the industry, while it has experienced some difficulties with the various provincial requirements, has not found these difficulties to be insurmountable and certainly has not found that they compare with some of the situations encountered in the United States. In comparing Provinces which regulate through commissions or boards, preference was cited for the Alberta Automobile Insurance Board because of its detailed knowledge acquired in dealing with only automobile insurance matters.

Ontario Now

At the present time, the government of the Province of Ontario does not have any formal mechanism to supervise or regulate automobile insurance rates in the Province. Mr. Justice Hodgins' recommendations, while they are contained in the Insurance Act, have never been proclaimed as law. The activities of the Provincial Superintendent of Insurance and the Federal Superintendent of Insurance with respect to the solvency of insurers under their jurisdiction do provide reasonable assurances that the consumer will be protected to the extent that claims, which are in fact submitted, will be paid. The bankruptcy and/or receivership experience of the Canadian insurance industry bears out the adequacy of this protection, since in recent history there have not been any losses of consequence. The Committee considered

the subject of solvency tests in its First Report and this topic is examined in Appendix I of the Second Report, on "Solvency and Liquidity Tests".

The Superintendent's Office also performs a variety of guideline tests or periodic analyses to ensure that insurance rates are not inadequate, are not excessive, and are not unfairly discriminatory. In general terms, the Superintendent's Office is able to satisfy itself that the public in Ontario is well served by having its automobile insurance rate levels determined by open competition in the market place.

However, in a recent memorandum submitted to the Committee, the Superintendent's Office described circumstances in which it was unable to arrive at a satisfactory agreement regarding proposed rate increases for 1976. In view of this experience the memorandum concluded:

"These circumstances seem to suggest that even though the present system will generally work extremely well, situations can arise which, notwithstanding public expectation, may be beyond the ability of the Superintendent and the Government to deal with promptly."¹

2. In The United States

The Legislation

"The regulation of the insurance business by the States was well-established by the late 1800's and continues today as the predominant form of regulation. The practice takes its point of departure from a series of court decisions and has been continued in the face of some contention that, because of the number of jurisdictions, insurance might better be regulated by the federal government. The classic case is *Paul versus Virginia*, in which the United States Supreme Court decided in 1868 that insurance is not a transaction of commerce and thus it can be neither interstate commerce nor subject to federal regulation. Until 1944, a period of 75 years, the *Paul* decision was upheld by the Supreme Court.

In 1941, complaints were made to the Department of Justice that certain insurance company practices were in violation of the Sherman Anti-Trust Act. As a result, a momentous 4 to 3 decision was handed down in 1944 by the United States Supreme Court before one of its largest audiences in history. This case, *United States versus Southeastern Underwriters Association et al*, known to the legal profession and to the insurance business as the *S.E.U.A.* case, held that insurance is commerce. Thus, because of its interstate nature, insurance would normally be subject to federal regulation.

1. Office of the Superintendent of Insurance, Ontario, Memorandum to the Select Committee on Company Law, "The need for a greater government presence in the determination of automobile insurance rates in Ontario", February 15, 1978.

As a matter of practice, because of delegation of authority by Congress, the regulation of the business of insurance remains a state function.

The specific delegation to the states of the power to regulate insurance occurred with the passage of Public Law 15 in 1945. Congress made the Sherman Act, the Clayton Act, and the Federal Trade Commission Act applicable to the business of insurance after January 1, 1948, "to the extent that such business is not regulated by state law". In other words, jurisdiction for regulating interstate insurance was left with the individual states as it had been for many years, but an important proviso was added that would permit the federal government to take over insurance regulation whenever the state regulation became inadequate".¹

In this way, Public Law 15, also known as the McCarran-Ferguson Law, ratified the state's power to regulate the field of insurance in the absence of specific federal insurance legislation. It provided anti-trust exemption for private concerted price fixing activities which were subject to state regulation. The Southeastern Underwriters decision had reversed previous U.S. Supreme Court decisions and subjected insurance to federal anti-trust laws. The McCarran-Ferguson Act actually was a form of compromise legislation in that it allowed the industry and its state regulators to pre-empt federal anti-trust laws with state regulation.

In order to comply with the McCarran-Ferguson Act, prior to January 1, 1948, all the states in the union had to legislate some form of regulation over insurance industries in that state. The primary objectives of rate regulation were that the rates should not be excessive, inadequate or unfairly discriminatory. In theory this meant that if the rating law was working as intended, there should be an adequate voluntary market at reasonable rates for insurance coverages which are widely purchased. Reasonable rates were taken to mean as low as possible without being inadequate. Inadequate rates could cause insurers to restrict the voluntary market by adopting more rigid rules for selection, to withdraw completely from the market, or to fail financially. Adequate rates were those considered necessary to attract investment capital. The adequacy of the voluntary market inferred freedom of choice among a considerable number of insurers.

Forms of Compliance

During this period of time, various types of state regulatory laws were legislated. A description of these various regulatory laws and an enumeration of the states opting for each type are contained as Appendix B. By far the largest majority of the states opted for some form of prior approval law. At the present time approximately two-thirds of the states in the United

1. D. L. Bickelhaupt and, J. H. Magee, *General Insurance*, 8th Edition, Richard D. Irwin, Inc., Homewood, Illinois, 1970, page 175 and 176.

States are using a form of the prior approval law. Under this form of rate regulation, insurance companies must file their request for rate modifications with the regulatory authority which then addresses the three questions previously mentioned: namely, are the rates adequate, are they excessive, are they unfairly discriminatory?

Only the statutory bureau laws and the state-made rate laws are considered by the industry to be more rigid than the prior approval laws. All three of these forms of regulation are said to interfere with the ability of the industry to provide insurance services efficiently and adequately. In general terms, the industry feels that rigid rate regulation has fostered the adherence to bureau rates, discouraged rate reductions, contributed to instability, established various forms of cross-subsidization between good and bad drivers, imposed unnecessary restrictions on collective merchandising and direct rating, and generally aggravated the availability problem.

Prior to January 1, 1948, advocates of the McCarran-Ferguson Act felt that open competition would result in excessive rates, price wars and mass bankruptcies; fears which constituted the rationale for state regulation and for the broad immunity from federal anti-trust provided by Public Law 15. In contrast to this concern, California enacted a competitive rating law in 1947 which provided for "open competition" in the California insurance market. Proponents of this legislation felt it fostered independent pricing, operating stability, pricing flexibility, and served as a more effective mechanism for accomplishing insurance goals: namely, a reliable insurance mechanism, generally available coverage, and a price reasonably related to cost.

The California regulatory system relies on market forces, it does not require advance or specific approval of rates, and it has no provision for filing by the insurer or rating bureau. California has concluded that open competition produces a rate structure which is responsive to costs. In addition, the open competition environment is said to encourage innovation in the form of coverage and rating plans, reduce residual market plans, enable new and small insurers to enter and succeed in the market place, and relieve regulators of the need to review filings thereby allowing them to examine actual pricing practices.

Policing of the industry in California is performed by the State Insurance Department through a programme of periodic rating and underwriting examinations for all insurers and rating bureaus operating in California. The costs of these examinations are borne by the organizations involved. Insurers are examined every five years or more frequently if required. The examination includes a study of the policy and endorsement forms, application forms, rates and rating procedures, statistical support for rates adopted, underwriting rules, and other matters considered relevant by the Insurance Department examiners. These examinations are performed by the rate regula-

tion division, and are separate and apart from reviews of financial condition performed by the field examination division.

California has in recent years examined the effectiveness of its insurance rate regulation procedures. Recognizing that the effectiveness of its insurance rate regulation procedures will depend upon many varying factors such as the quality and quantity of regulatory staff, the attitudes and priorities given by elected officials, and the effect of insurer and consumer attitudes on enforcement, California has concluded that its form of rate regulation continues to be the most effective mechanism for accomplishing insurance goals.

While no practical method of comparing the effectiveness of differing regulatory laws conveniently exists, regulators in California suggest that a few tests, when considered together, should indicate whether or not rate regulation is working satisfactorily from the standpoint of the insurer and the consumer. All of the tests performed by regulators in California were taken as measurements of the openness of competition in the insurance market place in that state. These tests included considerations such as the degree of market concentration by company or company group, price variations, ease of entry or exit from the market, economies of size, market growth, and solvency of insurers. The study "Competition under the California Rating Law—1974"¹ was performed by insurance department personnel and was supportive of the current activities of the department with respect to ensuring the adequacy of their open competition legislation. While their tests may have been rather simplistic from a statistical viewpoint, the results were borne out by further studies as will be indicated later in this study.

Recent Trends in the United States

In the last ten years in the United States, there has been a trend to open competition or various forms thereof. In other words, many of those states which originally selected a form of rigid prior approval law have been liberalizing these laws to facilitate independent pricing. Apparently recognizing the ineffectiveness of rigid regulation, approximately one-third of the states have now adopted some form of open competition law. The 1974 report of the National Association of Insurance Commissioners describes this occurrence as a classic reversal of position: "the industry which fought for the right to make and maintain rates in concert now wants rates subject to an open competition marketplace". The National Association of Insurance Commissioners supports price competition as a means of regulating insurance rates.

Two recent studies in the United States both support the benefits of competitive pricing or open competition laws as far as the regulation of au-

1. Borchert, L. O., "Competition Under the California Rating Law and its Effect on Private Passenger Automobile and Homeowners Insurance", Department of Insurance, State of California, 1974.

tomobile insurance is concerned. The Superintendent of Insurance of the State of New York, in his report entitled "Cartels versus Competition—A Critique of Insurance Price Regulation" stated that "the competitive pricing law has proved its worth. Its performance has been demonstratively superior to that of its predecessor, the pro-Cartel prior approval system. The law should be continued".¹

In January of 1977, the United States Department of Justice issued its report on "The Pricing and Marketing of Insurance".² The purpose of this study was two-fold. The study sought to determine whether state regulation provides benefits normally attributed to competition: namely, reasonable prices based on the cost of rendering services, efficient services rendered at lowest cost, and innovation. In addition, the study was to consider the impact of the U.S. Federal anti-trust legislation on the insurance industry if the present immunity provided by the McCarran-Ferguson Act was repealed.

The study examined the benefits of open competition laws, which have been demonstrated in California since 1947, in Illinois since 1969, in New York State since 1970. It commented that state regulators found themselves in a squeeze between the industry and the consumer in that they could not fulfill the statutory obligations required with respect to inadequate or excessive rates under the existing prior approval laws. In Illinois, the study noted that, in 1976, the Director of Insurance commented as follows, with respect to the effectiveness of the open competition/competitive pricing laws:

- He described a low population in the assigned risk plan.
- He observed a reasonable dispersement of price of coverages and diverse timing of price changes evidencing independence of pricing, innovation, experimentation and risk taking.
- He felt the insurers liked the system and he saw no diminuation in the market share held by smaller insurers. An increase in uninsureds was attributed to affordability problems.

This study was performed with reasonable sophistication and the Justice Department examined economic data on the effects of rate regulation in three jurisdictions: California, whose system has previously been described; New Jersey, which experiences substantial state involvement and minimal reliance on market forces in utilizing a prior approval system with a significant delay factor; and Pennsylvania, which has a prior approval system but differs from New Jersey in that its regulators permit higher rates for high risk drivers. The three states examined account for approximately one-fifth of the private passenger automobile insurance business in the United States.

1. State of New York, *Cartels vs. Competition—A Critique of Insurance Price Regulation*, 1975, page 88 and 89.
2. *The Pricing and Marketing of Insurance*, A Report of the U.S. Department of Justice to the Task Group on Anti-Trust Immunities, January 1977.

The study came to the following conclusions¹:

1. Rigid state rate regulation has had adverse effects in that evidence has shown that it has fostered greater adherence to bureau rates, discouraged rate reductions, contributed to operations instability, resulted in various forms of cross subsidization, imposed restrictions on collective merchandising and direct rating, and aggravated the availability problem.
2. Vigorous competition is consistent with a goal of reasonable prices. Evidence has indicated that competition fosters independent pricing and operating stability and flexibility in pricing; and that the relatively favourable performance of insurers under a highly competitive system suggests it accomplishes one of the basic insurance goals, that is, generally available coverage at a price reasonably related to cost.
3. The insurance industry could function effectively in a manner consistent with the federal anti-trust laws. It should be able to conduct its business without special exemption. It could pool its loss experience through bureaus and perform trending of future losses on a composite basis by advisory organizations. Anti-trust legislation would not prohibit insurance pools or re-insurance.
4. Vigorous competition is consistent with a goal of a reliable insurance mechanism. Experience has shown in the present competition states that unrestricted competition does not result in price wars and mass bankruptcies. The California experience has indicated that insolvency is a function of mismanagement. Rigid rate regulation has an adverse effect on stability and solvency in that it prevents insurers from readily adjusting rates to compensate for unforeseen conditions.
5. Competition suggests a need for a more effective system of solvency regulation, as in a fully competitive system inefficient insurers may fail. The transition to a fully competitive system may require a shift from "keeping every insurer afloat" to "swift detection and swift removal" of a failing insurer from the marketplace. The New York State Insurance Department has stated that objectives with respect to financial conditions must be balanced against their impact on the other goals of insurance regulation. The National Association of Insurance Commissioners has promulgated a need for a uniform early warning system which would monitor the financial condition of property and liability companies. Effective solvency regulation depends on the acceptance of market forces as a mechanism to weed out the weak and on a willingness to act. Therefore, there must be an established guarantee fund.
6. Competition is consistent with the goal of preventing unfair discrimination.
7. Special consideration is necessary with respect to invidious discrimination and the affordability problem. Federal standards are required to

1. *The Pricing and Marketing of Insurance*, A Report of the U.S. Department of Justice to the Task Group on Anti-Trust Immunities, January 1977, pages 340 to 348.

avoid invidious discrimination. The state should decide whether and how to provide direct subsidies to consumers who cannot afford price based upon cost.

8. The current residual market mechanisms are appropriate. Mandatory pooling will remain necessary to provide coverage to all who wish it and it should be at the alternative of the state.
9. Open competition as an alternative to the present restraints should be utilized in the pricing and marketing of insurance. The traditional public goals of insurance regulation, namely, reasonable prices, a reliable insurance mechanism, and economic and social fairness, can be provided by open competition and a competitive rating law. The industry would take advantage of the competitive market alternative.

In the light of these recent authoritative studies, a more detailed consideration of the various state regulatory laws would be of little use in comparing competitive rating laws to more restrictive laws for rate regulation.

3. Recapitulation of Canadian Versus United States Experience

The above history of insurance company regulation by government suggests somewhat of a contrast between the experience in Canada and the United States.

In Canada, the concern within the various Superintendents' Offices seems to stress the solvency rules, as most of the Canadian Provinces have not gone to great lengths at this stage to examine rates in a sophisticated fashion. While Canadian regulators pay heed to the inadequacy, excessiveness, or discriminatory nature of insurance rates, the formal thrust of their activities is to ensure that legitimate claims, when presented, will in fact be paid. Again, the bankruptcy and/or receivership experience of the Canadian insurance industry demonstrates the effectiveness of these activities.

In the United States, on the other hand, the formal concentration in governing the industry seems to be on the rate regulation side. Inadequate rates are only one of the several objectives of rate regulation. This apparently diffused thrust, as compared to Canada, theoretically should result in a broader measure of consumer protection, as it undoubtedly does in certain jurisdictions. However, the broader regulation followed by the American states has apparently created a greater insolvency risk, as evidenced by the number of liquidation and conservation proceedings currently being handled by the insurance departments of certain jurisdictions. Even California, whose ten point system was described by a Canadian insurer operating in that state as "more rigid than Canadian solvency rules", had sixteen resident insurers' estates in liquidation or conservation as at December 31, 1976. Similarly, the recent experience of the Government Employees Insurance Company (G.E.I.C.O.) is a good example of the failure of the government regulators to apply the regulations effectively and monitor the adequacy of rates.

The above review of Canadian and United States' experience with insurance company regulation indicates that perhaps attention in Ontario might be directed to providing a better balance between rate regulation and the surveillance of insurance company solvency. This matter is referred to further throughout the remainder of this study.

C. OBSERVATIONS ON THE ONTARIO SYSTEM

1. Responsibility for Rate Regulation

In the United States, those states without specific rate regulation for insurance companies come under the jurisdiction of the federal anti-trust laws for regulatory purposes; however, at the present time Illinois is the only such state. Much broader proposals for federal rate regulation in the U.S. are currently being considered and have been discussed for many years. However, the political, fiscal and social repercussions of federal regulation in the United States are immense. For example, replacement of tax revenues to the individual states poses, on its own, a mammoth problem. Legal precedent has firmly established state regulatory responsibility and the right to these revenues.

Under the Canadian constitution, the regulation of insurance rates appears wholly within the jurisdiction of the Provinces. As a general principle, The Combines Investigation Act provides that, if an industry is regulated by government in the public interest, then it is exempt from the provisions of the Act. The exemption, however, exists only for those matters which are specifically regulated and rate regulation must be in the form of rate approval or disapproval by the government.

This principle has apparently been carried forward in the new proposed federal "Competition Policy" legislation¹ which may, at some point, have an impact upon the operations of the insurance industry in Ontario, and upon the matter of rate regulation. There would appear, therefore, to be an opportunity for Ontario to pre-empt the proposed federal legislation if it was felt to be in the public interest to do so. At a minimum, the ramifications of this legislation would need to be identified to ensure that a duplication, or a void, in supervision or regulation does not result.

In the absence of specific rate regulation, the provisions of The Combines Investigation Act have applied to the insurance industry in this Province. However, regulation under The Combines Investigation Act has not prevented the development of certain issues which motivated the Committee to study the alternative forms of a government presence in the automobile insurance industry. Until the new proposed federal legislation is finalized and becomes law, it is not clear whether or not this legislation, any more

1. Bill C42—The Competition Act (now Bill C13—Competition Policy—Stage II).

than the previous legislation, would result in the improvements which may be considered to be necessary in Ontario.

2. Possible Shortcomings of the Present System in Ontario

Representatives of the industry in Ontario maintain that the present competitive nature of the market place ensures the best deal in terms of coverage and price for the consumer, and the industry also applauds the effectiveness of the present role performed by the Superintendent's Office. If regulation is deemed necessary by the legislators, then the industry hopes such regulation will take the most innocuous form from the point of view of interference with their operations.

Representatives of the Superintendent's Office have also expressed a general satisfaction with the present competitive system and also with the adequacy and effectiveness of their role in ensuring that the public in Ontario is well served by the automobile insurance industry. The Office has stated that it generally receives a high level of cooperation from the industry in finding solutions for specific problems. In addition and more to the point, representatives of the Office have indicated that the "watch dog" nature of its role generally acts as a deterrent to prevent the industry from abusing the primary goals of insurance.

Like its American counterparts, however, the Superintendent's Office understandably experiences considerable difficulty in determining whether or not a rate is inadequate or excessive. Such difficulties are to be expected in regulation, as most situations are different, must be examined on their individual merits, and the future consequences forecast.

In addition, the Superintendent's representatives have emphasized the vital importance of retaining a high degree of flexibility in any form of regulation, so as to facilitate the development of workable solutions to specific problems. According to representatives of the Superintendent's Office, rigid regulation in terms of formal specific tests and procedures will only compound these difficulties.

Both the industry and the Superintendent's Office agree, in general, that the service and protection offered the consumer by the competitive market place, that being the apparent situation in Ontario, is adequate; and that the present system achieves the primary goals of insurance, which are a reliable insurance mechanism, generally available coverage, and a price which is reasonably related to cost.

However, it has been suggested that there may be certain matters which perhaps cause the above conclusion to be less than convincing. These matters or concerns might be expressed as follows:

- (a) The results of the Superintendent's Office's efforts with respect to its monitoring of insurance company solvency are well known and clearly

demonstrable. However, on the broader issue with respect to "helping people get the most insurance for their money . . . in simple words, . . . the public purpose of insurance regulation"¹, its activities are not readily apparent.

Existing regulatory legislation has never been proclaimed as law. As a result, the activities of the Superintendent's Office with respect to the supervision of automobile insurance rates are not obvious in the absence of a periodic reporting of compliance. Presumably, however, this Office has done a creditable job, otherwise public reaction would have demanded change.

- (b) "A system of regulation that relies on competition is valid only where competition exists."² While effective competition may in fact be prevalent in Ontario, it is difficult to identify the emphasis placed upon determination of its existence by the Superintendent's Office, the investigation and analysis work performed in making such a determination, and the frequency of such reviews.

Accordingly, the following considerations arise in reviewing the current system in Ontario:

- (a) If a competitive insurance environment in Ontario is considered to be the best means of ensuring an insurance system that serves the public interest, then the following questions become relevant:
- What criteria constitute a competitive or open market place as far as the provision of automobile insurance by private insurers is concerned?
 - How can this market place be monitored in the future to ensure it retains its competitive characteristics on an on-going basis?
 - Whose responsibility is it to make such a determination and to provide the on-going monitoring capability?

These questions are examined in Section D of this study.

- (b) If regulation is to extend beyond the monitoring of competition to government supervision of rates in the public interest, then additional or perhaps alternative questions must be addressed:
- What are the alternative methods of providing an increased governmental role in the regulation of automobile insurance rates?
 - Can the existing in-house rules and procedures be relied upon to provide effective safeguards to the public interest, or is there a need to provide legislative sanction for these rules and perhaps for additional safeguards?

1. State of New York, *The Public Interest Now in Property and Liability Insurance Regulation*—A Report to Nelson A. Rockefeller by the State of New York Insurance Department, 1969, page 12.

2. *Ibid.*, page 17.

- Is there a need or justification for more to be done to protect the public interest in the matter of the financial stability of insurers?

These questions are addressed further in Section E of this study.

Accordingly, the remainder of this background study is devoted to a consideration of some possible answers to the above-mentioned questions. In structuring these questions, a distinction has been made between monitoring competition and more stringent regulatory practices and procedures. It is also worthwhile to consider a combination of the two as an alternative that might be suited better to meet Ontario's regulation requirements.

Conceivably, many of the above questions are broader than automobile insurance and could also be asked about general and other insurance carriers. In arriving at solutions to these questions, attention might be paid to the achievement of a "better balance" between the goals of financial stability of insurers and the other goals of rate regulation.

D. COMPETITION AS A POSSIBLE FORM OF REGULATION IN ONTARIO

1. What Criteria Constitute a Competitive or Open Market Place as far as the Provision of Automobile Insurance by Private Insurers is Concerned?

If regulation in Ontario is to be flexible and rate determination is to be left largely to competition in the market place, then the question arises as to what criteria constitute a competitive or open market environment. This topic has been studied in depth by governments and regulators in other jurisdictions in Canada and the United States. This section will outline relevant considerations which have been addressed by two reviews of the extent of competition in the insurance industry in Canada.

Findings of the British Columbia Royal Commission on Automobile Insurance

The Royal Commission on Automobile Insurance in British Columbia in 1968 considered the matter of competition in the automobile insurance industry in that Province. It outlined the following requisites for perfect competition:

- “1. Each buyer and seller in the economy be so small in relation to the entire market that he cannot influence price.
2. Perfectly standardized commodity and the absence of any other reason for the preference of one seller or buyer over another.
3. Perfect knowledge and foresight and the absence of uncertainty.
4. Freedom of entry into the industry and exit therefrom with perfect mobility of all of the factors of production.
5. Cost relationship consistent with the continued existence of many sellers.

These conditions taken together would produce an instantaneous mutual adjustment of supply and demand resulting in the efficient use of resources at all times."¹

Recognizing that theoretical "perfect competition" is unattainable, the Commission considered the standard of "workable" or "effective" competition as developed by economists. The factors usually taken into account to determine "workability" are the *structural characteristics* of the industry, the way in which competition is *conducted*, and the *performance* which results from the interaction of the structural and conduct factors.

In the perspective of the insurance industry, *structural factors* examined by the Royal Commission included:²

- The number of sellers in the market, their size relative to one another and their ability to compete. The number of firms must be large enough to provide customers with alternate sources of supply; no firm or group of firms acting in concert should be able to exercise monopoly power for long; the more firms the better; high levels of concentration may be quite compatible with effective competition if other factors are favourable.
- The ability of new firms to enter freely and compete with existing firms on a profitable basis; potential entry, not actual entry is important.
- The existence of incentive for firms to undertake competitive moves, price cuts, product improvements, or innovations in the production or marketing process.

Conduct requirements considered relevant by the Commission included:³

- Independent behaviour. Firms must behave independently, each seeking to improve its profits; it is not necessary for all firms to behave in this manner.
- An absence of actions deliberately aimed at excluding present or potential competitors or at restricting their ability to compete.
- Evidence of active price competition. Price leadership by one firm may be evidence of the absence of price competition; a large single seller may take the initiative and the rest follows; a similar umbrella may be afforded by a government authority professing to regulate prices.
- Nature and extent of product differentiation. A driving force behind improved products and economic progress generally is the search for a temporary monopoly through product differentiation,—such action is considered to be beneficial.

1. Province of British Columbia, *Royal Commission on Automobile Insurance in British Columbia*, 1968, page 291.

2. *Ibid.*, pages 294-295.

3. *Ibid.*, pages 296-298.

Market performance criteria included:¹

- Suspect performance: when the performance record, in response to growing demand, is one of rising prices rather than increasing output.
- Impressive performance: when the record is one of introducing cost reducing innovations permitting the cutting of prices and growth with the market.
- Truly administered price: where the price is set and is totally unresponsive to supply and demand changes; this is incompatible with effective competition.
- Unfair price discrimination: charging the same price for two identical policies of insurance where the hazard can reasonably be identified as different; on a continuous and regularized basis this is evidence of the existence and exercise of monopoly power.

The Royal Commission, after its consideration of the above factors, concluded that in British Columbia:²

- Premiums were standardized over 80% of the market. Uniformity in price was much more pronounced after the formation of I.B.C. The price leadership role of I.B.C. tempered what competition did exist. Under the I.B.C. price umbrella there was no need to reduce prices.
- Absence of effective competition was indicated by the finding that average company expenses were lower than allowed by the then current two-third loss to one-third expense ratio.
- Present failure of most companies to allocate their expenses by line was an indication of ineffective competition.
- A tight market situation and overutilization of the Assigned Risk Plan was evidence of ineffective competition. The very existence of the plan was taken as indicative of a failure of competition to function effectively, that is, an inability to price commensurate with the hazard.
- Little evidence was shown of the use of rating structures which would tend to force rates into proportionality with marginal costs for individual classes.
- Industry's low rate of productivity increase was an indication of a state of competition too comfortable to be effective.

Accordingly, the Royal Commission on Automobile Insurance came to some rather harsh and *negative conclusions about the insurance industry's performance in British Columbia in the years prior to 1968.*

1. Province of British Columbia, *Royal Commission on Automobile Insurance in British Columbia*, pages 298-301.

2. *Ibid.*, pages 381-386.

Findings of a Study for the Insurance Bureau of Canada

To appreciate the impact of judgement and the difficulty in evaluating the effectiveness of competition in a market place, it is useful to contrast the findings of the 1968 British Columbia Royal Commission, with those of Professor Quirin et al. in their 1974 study of the national insurance market place, which was performed for the Insurance Bureau of Canada.¹

Similar to the B.C. Royal Commission but in far greater statistical detail, the Quirin study considered the criteria for competitive effectiveness to be based upon the "*structural features and aspects of competitive behaviour* (wherein) *the object of concern is the ultimate performance of the industry*".² Specifically, the structural evidence examined by this study encompassed the extent to which output is concentrated among a small group of firms, changes in the extent of concentration, and changes in the stability of market shares of leading firms. In addition, the study addressed the degree to which potential competition was enhanced or inhibited by difficulties in entering the market and it examined the relationship of costs to scale of operation.

As far as competitive behaviour was concerned, the study commented that: "the character of competition is dependent upon how the competitors behave . . . cooperative price fixing is of concern here".³ In this regard, the marketing practices and price setting mechanisms used by the insurance industry were examined, the key issue being whether or not the prices which emerge from the competitive process bear an appropriate relationship to marginal costs of production, that is, price of each commodity equal to the addition of the producing industry's costs.

Under each of the major components of *structural evidence*, the Quirin study of the national market found as follows:⁴

Market Concentration

- Market positions of leading firms had changed several times, often drastically, over the study period;
- Low concentration and fluid market positions were consistent with the hypothesis of effective competition;
- The importance of rating bureaus along with their members' market share declined dramatically; bureau members' rates deviated from bureau rates to an increasing degree and with increasing frequency; bureaus fell far short of constituting effective cartels;

1. G. D. Quirin et al., *Competition, Economic Efficiency and Profitability in the Canadian Property and Casualty Insurance Industry*, Insurance Bureau of Canada, 1974.

2. Ibid., page 17.

3. Ibid., page 18.

4. Ibid., pages 19-33.

- There was no evidence of greater rate uniformity after I.B.C. than before;
- Effective concentration was lower than most Canadian manufacturing industries and market shares of individual organizations were unusually flexible.

Entry and Exit

- Entry barriers appeared unimportant;
- Product differentiation was insignificant so existing firms had little advantage over newcomers;
- Independent agency marketing network worked to reduce cost of access;
- Licencing requirements were not onerous or overly costly from an equity requirement viewpoint;
- Growth was restrained by the solvency rules and accounting technicalities, but was not particularly serious;
- Entry/exit statistics over the study period confirmed the above assessment;
- Barriers to entry/exit did not have a significant impact on competitive possibilities in the industry.

Economies of Scale

- Appeared very small in the industry.

In conclusion on the matter of *structural evidence*, the study found the industry to be relatively unconcentrated; market shares of leading insurers to be quite unstable; entry into and exit from the market place to be unimpeded; and no evidence of significant economies of scale, at least in the administrative operations. It felt the position of the rating bureaus to be ambiguous, and indicated that they should be judged on their contribution to the competitive process, rather than on their mere existence and on the members' tendency to agree on prices. In addition, the study felt that the competitive initiative had passed from the bureaus during the study period.

As far as *competitive behaviour* was concerned, the study observed that the existence of some degree of similarity in the classes used for ratemaking purposes, and the fact that statistics became available to all simultaneously, produced the appearance of a concerted action on prices by the members of rating bureaus. This was viewed as an anti-competitive threat only if the bureaus imposed essentially monopolistic prices on their members and these imposed prices were followed to a significant degree by non-members. However, the study concluded that the bureaus had no power, of any consequence, over members and even less over non-members. The study acknowledged a possibility of power of persuasion and example, but after examining the role of price deviators from bureau rates, concluded that the

influence of these deviators was significant enough to enforce effective price competition in the then current market. In viewing the marketing practices followed by the industry, the study thought that there appeared to be some direct or indirect concerted behaviour among members of rating bureaus with respect to commission levels.

Among other things, the Quirin study felt that the evidence examined supported the conclusion that "*competition within the industry is effective within the limits imposed by the legal framework within which it operates.*"¹ It found the industry to have a relatively fluid market structure in which no firm exercised any monopolistic power. Cost characteristics supported effective competition, as did price competition, which had led to the development of more sophisticated rate structures and reductions in unit operating costs which had been passed on to the consumer. Returns on equity investment were found to be commensurate with the risk. Non-members of rating bureaus had assumed a significant pricing initiative role, and the then present bureaus were responding to change rather than initiating it. Because of the regulatory process in existence, the study felt that certain restrictions had evolved in the distribution system. *No evidence, however, suggested that the abandonment of primary reliance on the competitive mechanism would lead to an improvement in performance.*

Summary

In outlining the consideration given to the subject of competition by the British Columbia Royal Commission, and the viewpoint expressed by the Quirin study commissioned by the Insurance Bureau of Canada, it is the intention of this background study to provide some benchmarks which are considered by others to be meaningful measuring sticks that may be used to assess the effectiveness of competition in an insurance market place. In addition, the foregoing discussion illustrates the breadth and complexity of such an assessment and the role which judgement can play in specific determinations.

If it is decided that a greater government profile is required in the regulation of automobile insurance rates in Ontario and the trends in other jurisdictions against rigid regulation are followed, then a determination of the effectiveness of competition must be made. A detailed consideration of the effectiveness of competition in the automobile insurance market in Ontario is, however, beyond the scope of this study; instead, an excellent summary of the economic theory of an evaluation of effective competition, taken from the deliberations of the National Association of Insurance Commissioners in the United States, is included as Appendix C, Tables 1 and 2 to this study.

1. G. D. Quirin et al., *Competition, Economic Efficiency and Profitability in the Canadian Property and Casualty Insurance Industry*, Insurance Bureau of Canada, 1974, page 74.

2. How Can The Market Place be Monitored in the Future to Ensure it Retains its Competitive Characteristics on an on-going Basis?

Once the criteria constituting effective competition in the insurance market place have been identified and defined, and some sophisticated determination has been made of the present condition of the Ontario market place, it may then be necessary to ensure that appropriate procedures are put in place to monitor this market place in the future. In order to satisfy the protection of the public interest, this monitoring process may require a periodic public reporting procedure.

The development of the monitoring procedures will, to a large extent, be determined by the nature of the defined competitive characteristics. These procedures could outline the nature and extent of the tests and reviews to be applied, and the frequency of their application. Included as tests might be a periodic consideration of the structural, behavioural, and performance factors outlined in the preceding section, assuming these to be meaningful in an Ontario environment. In addition, supplementary reviews which include the size of the residual market, a market sampling of availability, and a comparison of rates offered might be considered as periodic key indicators of the effectiveness of competition. Other tests, such as the level of profits or profit trends and return on investment could also be included. Likely the monitoring function should involve several tests or benchmarks in order to allow the application of judgemental factors: one or two major tests could be too rigid or restrictive.

The terminology "monitoring competition" suggests a formal structured process followed by regulators which includes appropriate reportings at regular intervals. The National Association of Insurance Commissioners in the United States has developed such a monitoring plan which is outlined in Appendix C, Table 3. In Ontario at the present time, market factors are periodically examined by the Superintendent's Office on an informal basis. Regular formal monitoring and the identification of trends might be more useful and could be compared against benchmarks developed in a broader periodic assessment process.

With the passage of time, and perhaps the enactment of the federal "Competition Policy" legislation, the monitoring process could become less meaningful or even redundant in Ontario. Accordingly, sufficient flexibility should be afforded in the mechanism to permit change or alternate forms of supervision, should circumstances warrant future changes. In California, for example, it appears that state officials, having satisfied themselves over the years as to the effectiveness of California's competitive rating laws, presently monitor the relevant insurance market place on an "exception" or "complaint" basis, which is periodically supplemented by an in-depth insurer review.

While a competitive environment and monitoring process may already exist in Ontario, it does not appear that the Superintendent's Office presently views itself as primarily engaged in a monitoring role. The role of monitoring competition would appear, however, to provide broader safeguards to the public interest than the exercise of the traditional solvency role alone.

3. Whose Responsibility is it to make a Determination of the Existence of Competition and to Provide an on-going Monitoring Capability?

The peculiarities of the insurance market place and the complexity of its product might make it appropriate for the same regulatory mechanism to perform both the initial and on-going evaluation of the effectiveness of competition. In addition, these activities should dovetail with any relevant provisions of the proposed new federal "Competition Policy" legislation which may ultimately provide federal determination and monitoring of competition, rates, and other matters in the insurance industry in Ontario.

This study has outlined the difficulties and complexities of the process of monitoring competition; the specialty actuarial, legal, economic and financial skills required to perform the job adequately; and the mechanisms, procedures, and recommendations considered or followed by other jurisdictions in Canada and the United States. In Ontario, a monitoring role could be established within the Superintendent's Office, or it could be delegated to some other government body such as a Public Utilities Board or a separate automobile insurance board.

Can the role of monitoring competition be accommodated by the Ontario Superintendent's Office, given the present responsibilities and operations of that Office? Whether or not this Office, as presently staffed and organized, could accept additional work loads is a matter which cannot be properly addressed until the specific requirements are defined. Only then can the necessary numbers of staff and diversity of skills be determined. A brief review of the present staff mix and responsibilities of the Superintendent's Office is provided in Appendix J to the Committee's Second Report.

If the role of monitoring competition is to be accommodated outside the Superintendent's Office, responsibility for this role might be transferred to a separate automobile insurance board or to a Public Utilities Board. The specialized knowledge acquired by a separate board would seem to provide an advantage over monitoring by a Public Utilities Board which has other responsibilities. This matter is discussed again in Section E of this study.

Of overriding concern in the choice of a monitoring mechanism would be the question of cost and benefit in terms of the public interest. Clearly, little would be accomplished if significant incremental costs of monitoring did not result in the provision of a more reliable insurance mechanism which

was available to all and at a price in reasonable proportion to cost. It might, however, be difficult to prejudge whether the benefits of a particular regulatory approach would outweigh the costs. In such a case it might be preferable to avoid any cumbersome regulatory mechanism until simpler regulatory approaches have proven to be ineffective.

E. OTHER FORMS OF GOVERNMENT REGULATION AS POSSIBLE SOLUTIONS FOR ONTARIO

The preceding section of this study concentrated on the alternative of open competition which is becoming more common as the preferred regulatory form in the United States. Open competition is endorsed as the most effective regulatory approach by a variety of authoritative sources and is probably the most capable of implementation in Ontario via legislation or expanded in-house mechanisms, with a minimum of disturbance to the industry and the regulators. Implementation could be effected in principle by expanding the present in-house guideline tests carried out by the Superintendent's Office or it could be achieved by legislating a competitive rating law or some form thereof.

1. What are the Alternative Methods of Providing an Increased Governmental Role in the Regulation of Automobile Insurance Rates?

As an alternative to the open competition form of regulation, more restrictive methods of rate regulation can be implemented to provide an increased government role in protecting the public interest. Alternative methods of providing government involvement in the regulation of automobile insurance rates include a *public utility concept*, that is, the concept of justification of rate changes before a separate automobile insurance board or public utilities board, as adopted in several Canadian jurisdictions; legislated responsibility for some *government department or agency to set automobile insurance rates*; or *government ownership*, as practised in four jurisdictions in Canada.

With regard to the *public utility concept*, licenced insurers might be required to file applications for rate increases with a Public Utilities Board and justify them based upon increased costs in much the same way as regulated utilities do. Effective implementation of this concept, however, would require the standardization of products which might be achieved only with considerable difficulty.

Where a board concept is utilized, preference has been expressed by the industry for a *separate* automobile insurance board. The specialized knowledge acquired by a separate board is said to provide for more efficient processing of rate applications than is provided by those public utility boards which have been delegated this responsibility in some Canadian jurisdic-

tions. On the other hand, board members are sometimes said to be subject to political pressures that impair their objectivity. This objection has been raised primarily in the United States. Critics of the board concept also assert that a regulatory board may unduly increase consumer expectations for lower rates.

The second alternative of *rate setting by a government department or agency* also contains many potential problems depending upon the specific mechanism selected to implement such a scheme. Some have argued that rate setting by a government department or agency might be inconsistent with the public interest in that it could increase insurance costs to consumers, cause a possible reduction in services, or force unwanted services on the consumer.

Factors that have been described as arguing against rate setting by government include the following:¹

- The regulated companies could in fact be better off under such a scheme, because rates would likely be set at levels where the most inefficient companies could realize a profit. "Creaming" by the more efficient insurers could result.
- A standardization of product (risk classes) would be required. This has a potential for creating downline problems because of inflexibility.
- Rate setting requires control over the level of service being offered. Accordingly, the associated practical problems of monitoring uniform claims settlement procedures, ensuring broad geographical distribution, etc. must be dealt with.
- If risk classes were eliminated and automobile insurance provided in a fashion similar to health insurance, costs would likely escalate beyond reasonable levels because consumers would have little incentive to reduce their losses.
- If controls were placed on the levels of return on investment or profits, similar to Anti-Inflation Board requirements, the traditional difficulties in defining returns and profits would emerge. In addition, profits or return on investment form a very small part of the cost to the consumer and controls on this component could create future difficulties in attracting new capital to the industry, potentially leading to capacity problems.
- If controls were placed on the upper limit of rates and insurers were permitted to charge less, little incentive would be provided for them to reduce costs. In periods of rising costs, such regulation could result in increases to the residual market, cancellations or non-renewals, and could generally aggravate the availability problem.
- As a practical problem, who would set the rates and provide the functions presently supplied by the industry and what assurances would be

1. Proceedings before the Select Committee on Company Law. Remarks by Mr. Peter Alley, Assistant Professor of Business Administration, York University, September 5, 1977.

provided that they could perform a better job than is presently being achieved?

The above cited factors do not necessarily negate the alternative of government rate setting, but they impose constraints on the insurance industry which might in some cases be against the interests of the insured public.

A third alternative for increased government involvement in rate regulation is *government ownership*. This alternative is reviewed at length in the second background study to this Report. In Saskatchewan, Manitoba, and British Columbia, rates for basic compulsory coverage are set by the government corporation. Private insurers are allowed to compete for extension coverage but their market share is small. Accordingly, no further regulation of rates is required.

2. Can the Existing in-house Rules and Procedures be Relied upon to Provide Effective Safeguards to the Public Interest, or is there a need to Provide Legislative Sanction for these Rules and Perhaps for Additional Safeguards?

Ontario is one of the few jurisdictions which thus far has not legislated or proclaimed any regulations pertaining to the supervision of automobile insurance rates.

Sections 365 to 367 of the Ontario Insurance Act have never been proclaimed as law. These sections provide for an information filing of rates and changes to rates by rating bureaus and insurers, and they would give the Superintendent the authority to inquire into rates and supporting information. In addition, the Superintendent could order an adjustment to the rates for automobile insurance if the evidence showed that such rates are "excessive, inadequate, unfairly discriminatory or otherwise unreasonable".

At the present time, most rating bureaus and insurers file their rates with the Superintendent's Office on a courtesy basis. Presently, when information comes to the attention of the Superintendent, either from the work of his staff or as a result of a complaint from the market place, indicating that the rates charged by an insurer are inconsistent with the above criteria, his Office has been able to rectify the situation by meetings and discussions with the parties concerned. In addition, anomalies in the market place have been solved by the joint cooperation of the Superintendent's Office and the industry. Should an increased government presence in the supervision of automobile insurance rates be considered to be necessary, legislative sanction might not be required; instead the government presence could be accomplished by suggesting amendments to the Superintendent's "in-house" rules and procedures.

If it is decided that new legislation is required, then a choice must be made between the more restrictive forms of legislation, such as prior ap-

proval laws found in some jurisdictions of the United States and outlined in Appendix B; and other non-restrictive regulatory laws such as those in use in several Canadian jurisdictions and in a number of U.S. states. Considerable evidence has been collected in the United States which suggests that "restrictive" laws and perhaps even many of the less restrictive laws are no longer suited to conditions in the industry; since these laws were enacted, "the property and liability insurance business has refined its pricing and underwriting methods, has grown and become more sophisticated, is exhibiting more diversity in price and distribution, and manifests a real willingness to compete in price".¹ Accordingly, it may be more appropriate for Ontario to direct its attention to examining critically the merits of competitive rating legislation.

Appendix D to this study provides some examples of legislation from other jurisdictions. Included is a model Competitive Rating Bill which was developed recently by the American Insurance Association in conjunction with broad industry support. Applicable to most general insurance lines, it provides for a use and file system and is intended to foster competition. Appendix D, Table 2, reproduces Section 321 of the Alberta Insurance Act (enacted in 1971) which provides for the creation of the Alberta Automobile Insurance Board and sets out the regulations to be followed by automobile insurers in that Province. The regulatory system utilized is prior approval but with a sixty day deemer provision that provides a relatively non-restrictive form of regulation. Alberta has served as a pattern for the recent amendments to the legislation in Newfoundland and New Brunswick.

3. Is There a Need or Justification For More to be Done to Protect the Public Interest in the Matter of the Financial Stability of Insurers?

Early Warning System

As already stated, Canadian jurisdictions have established an admirable record as far as their monitoring of the solvency of insurers is concerned. However, the increasing complexity of modern business and the Committee's strong recommendations calling for a review of the industry's present conservative investment policies² suggests that more might be done in the future to keep this record intact.

Over the past five years, the National Association of Insurance Commissioners in the United States has developed and implemented an early warning system currently utilized by a number of state regulators. The purpose of this computerized system is to permit regulators to identify those property and liability insurers needing more careful analysis and surveil-

1. State of New York, *The Public Interest Now in Property and Liability Insurance Regulation*. A Report to Governor Nelson A. Rockefeller by the State of New York Insurance Department, 1969, page 16.

2. Select Committee on Company Law, *First Report on Automobile Insurance*, 1977, pages 127 and 128.

lance. The system is comprised of a series of financial tests and ratios which, when applied to the operating results and financial position of the insurer and the results compared to a predetermined set of criteria, allow some conclusions to be drawn with respect to the insurer's financial condition. While the early warning system is still in its infancy and steps are being taken to improve the currency of information and test results, preliminary conclusions by regulators indicate the system to be effective in some areas. By analyzing the test results of insurers who subsequently became insolvent, regulators are now obtaining results which will allow them to firm up or refine their predetermined criteria and develop more specific plans to deal with insolvency situations in the future. More detail is provided on the N.A.I.C. Early Warning System in Appendix E.

The Superintendent's Office has reviewed this system and its relevance to Ontario. Certain of these tests have been modified in order to accept a Canadian form of reporting and are actually utilized to supplement the traditional "in-house" solvency tests. Based upon experience to date, representatives of the Office indicate that the results from using the N.A.I.C. tests have merely served to confirm information already apparent from the more traditional solvency reviews or other procedures used to monitor the financial condition and performance of Ontario incorporated insurers.

Consideration might be given to including the Early Warning System, assuming it to be adaptable and compatible with Canadian requirements, into whatever monitoring mechanism might be established in this Province. This will be particularly true as N.A.I.C. continues to improve and refine the system and additional adherence and experience is gained in the United States.

Guarantee Funds

About twenty states in the United States have legislation which stipulates that all insurance companies operating in the state must provide funds for the protection of policyholders in the event of an insurance company insolvency.

These laws normally provide that the industry will be subject to assessments on the basis of premiums written when funds are required to satisfy claims against an insolvent company. The rescuers then are allowed in turn to assess their own policyholders, presumably in the form of increased future premiums. Some states, however, such as New York, have a "pre-funded" variety of guarantee fund where contributions are provided in advance on some estimated basis.

Canadian jurisdictions do not have similar legislation with respect to the insurance industry. In Ontario, farm mutuals are required to maintain a guarantee fund but the fund was originally established for different reasons. Other regulated or semi-regulated industries are required to contribute to and

maintain guarantee funds for the expressed purpose of providing protection against the losses from the insolvency of one of its members: for example, the credit union industry is required to maintain a stabilization fund in some Canadian jurisdictions.¹ At the present time, in the event of an insurance company insolvency in Ontario, unearned premiums and unpaid claims and benefits to policyholders would rank as unsecured. If a shortfall was experienced on asset realization, these claims could go unsatisfied.

In addition to the Early Warning System outlined above, consideration might also be given to the need for a guarantee fund in Ontario as a form of consumer protection in the future. Further investigation of the guarantee fund concept and operation is required before final conclusions may be drawn. It is significant to note, however, that the "prefunded" variety of guarantee fund created substantial potential problems for the State of New York. Administered by state regulators, the assets of this fund were committed in such a way as to prevent the default of several of the State's agencies. Accordingly the fund's assets were not available to the task force which was working diligently to prevent the collapse of G.E.I.C.O.

A different type of complication arose in some other states in which G.E.I.C.O. operated. These were states which had established a Fund that relied on assessments made subsequent to the occurrence of an insolvency. Regulators and the industry in these states were faced with a potential "domino effect" of additional insolvencies which conceivably could have been initiated by a major insurer failure.

1. As to the use of guarantee funds by deposit insurance corporations in the case of loan and trust corporations, see the Report of the Select Committee on Company Law on *Loan and Trust Corporations*, 1975, William Hodgson, M.P.P. Chairman, Chapter 17, Section 17.02.

APPENDICES

APPENDIX A	Rate Regulation in Canada
Table 1	Provinces with Rate Regulatory Provisions
APPENDIX B	State Rate Regulatory Laws Applicable to Automobile Insurance
Table 1	Classification of States by Type of Rate Regulatory Law Applicable to Automobile Insurance
Table 2	States with Competitive Rating Laws
APPENDIX C	Monitoring Competition: A Means of Regulating the Property and Liability Business—N.A.I.C.—1974
Table 1	The Competitive Market as Viewed by the Economist
Table 2	Economics and the Insurance Industry
Table 3	Monitoring the Efficacy of Competition as a Regulator of Rates
APPENDIX D	Sample Legislation
Table 1	Competitive Rating Bill
Table 2	Extracts from the Insurance Act of Alberta
APPENDIX E	The Early Warning System—N.A.I.C. Regulatory Tests for Property and Liability Insurers
APPENDIX F	The Insurance Act—Sections 365-367 Pertaining to Rate Regulation

RATE REGULATION IN CANADA

Regulation Authority	ALBERTA		NEWFOUNDLAND		NEW BRUNSWICK		NOVA SCOTIA	
	Alberta Automobile Insurance Board (3 member)	December 1971	Board of Commissioners of Public Utilities (4 member)	June 1977	Board of Commissioners of Public Utilities (7 member)	February 1976	Board of Commissioners of Public Utilities (9 member)	1964
Appointment	Prior Approval, 60 day deemed clause		Prior Approval, 60 day deemed clause		Prior Approval, 60 day deemed clause		File and <u>use</u> , file at least 10 days before use	
Type of Regulatory law								
• Powers and objectives	<ul style="list-style-type: none"> - Objective to play a watchdog role over the rates charged for compulsory coverages. Also authorized to investigate any aspect of auto insurance including availability and benefits 	<ul style="list-style-type: none"> - Power of general supervision of the rates an insurer charges or proposes to charge for automobile insurance - Patterned after Alberta law 	<ul style="list-style-type: none"> - Power to approve, prohibit or vary any rate change - Patterned after Alberta law 	<ul style="list-style-type: none"> - Role of the Board is to monitor automobile insurance rates. Power to inquire into rates and require their adjustment if they are excessive, inadequate, unfairly discriminatory or otherwise unreasonable 				
Procedure	<ul style="list-style-type: none"> • Board receives applications from insurers for establishment of rates or revision of those previously approved • Board reviews actuarial evidence included in application, and if proposed rates are appropriate, approval is granted • If the Board rules that rates are unjustified, it may request applicant to attend a Board meeting, or it may convey non-approval, and name, instead, specific rates that are approved • Rates not approved or prohibited by the Board within 60 days are deemed to have been approved 	<ul style="list-style-type: none"> As in New Brunswick 	<ul style="list-style-type: none"> • Board receives applications for rate approval and sets a date for public hearing • Applicants present evidence and answer Board questions • Board meets after hearing, and may decide immediately to approve or prohibit, or may defer decision subject to additional reports by the consulting actuary • Rates not approved or prohibited by the Board within 60 days are deemed to have been approved 	<ul style="list-style-type: none"> • Insurers file rate schedules with the Board at least 10 days before intended effective date • Rates are automatically effective on date specified in filing without any action on the part of the Board • The Board is empowered to request further data at any time, to review rates, and to require their adjustment after a hearing in accordance with the criteria set out in the Insurance Act • Board issues periodic reports with respect to their analysis of the rate schedules filed 				

Actuarial Assistance	Consulting Actuary	Consulting Actuary	Consulting Actuary	Consulting Actuary
Compliance	<p>No direct policing is undertaken. A fine of up to \$5,000 is applicable for non-compliance; licence of the insurer may be suspended or cancelled</p> <ul style="list-style-type: none"> 1976 - 136 applications 1977 - 90-100; 16 deferrals due to incompleteness or unjustifiable rates Time span from filing to approval is, on average, 25-40 calendar days 	As in Alberta	As in Alberta	As in Alberta
Applications Received and Time Span From Filing to Approval		<p>Limited number - Board has functioned only since June 1977</p> <ul style="list-style-type: none"> 1976 - 3 public hearings/78 applicants (52 using I.A.O. rates) 1977 - 3 public hearings/42 applicants (33 using I.A.O. rates) 1976 filings required 14-2 months for decision; in 1977 decision on some filings took 3 months due to disagreements No disapprovals to date, but applicants have made adjustments 	<ul style="list-style-type: none"> 1976 - 70 to 72 companies have filed rates No delay, rates effective in most cases 10 days after filing No adjustments made by Board to date 	
Intended Improvements	None	<ul style="list-style-type: none"> Will attempt to set a base rate <ul style="list-style-type: none"> Intent would be to automatically approve a certain percentage above or below the benchmark A uniform classification system might be required 	<ul style="list-style-type: none"> Need for Board and the industry to reach agreement on the objectives of rate setting and the methods of calculating reasonable rates 	<ul style="list-style-type: none"> Board will continue to demonstrate its monitoring role by issuing reports analyzing rates filed. The onus will remain on the industry to meet standards of the legislation
			<ul style="list-style-type: none"> Trend to request applicants to base loss experience data on New Brunswick only (difficult when N.B. is only 3% of total Canadian market) 	<ul style="list-style-type: none"> Board has requested major companies to submit supplementary information re: loss experience, expense loading factors etc. More in-house staff needed for monitoring role

APPENDIX B

State Rate Regulatory Laws Applicable to Automobile Insurance

DEFINITIONS

Competitive Rating Law

A law permitting insurance companies to put revised rates into effect without prior approval of the state regulatory agency, and prohibiting rate agreements among insurers.

No Rating Law

No laws directly control specific rates, but ratemaking is subject to the provisions of state anti-trust laws.

No-Filing

There is no requirement that rates be filed or that affirmative approval by the Insurance Commissioner be granted before rates are used. Rates adopted may be put into effect immediately. Regulatory authorities periodically supervise adopted rates to ensure that they comply with the standards of the rate statute.

Use and File

Rates are effective immediately, but must be filed at a future specified date with state regulatory authorities for information purposes.

File and Use

Rates are effective immediately upon filing, unless a specified waiting period or future effective date is prescribed by the law. Rates are subject to review and possible disapproval after they have been put into use. This form of regulation is often referred to as "subsequent disapproval".

A file and use law may be so administered as to make it, for all practical purposes, the equivalent of a prior approval law.

Prior Approval

Rates must be filed with the Insurance Department and must be approved before use. In some states a waiting period applies, during which period the filings are reviewed. Rate filings not disapproved within the waiting period are deemed to be approved. Rates put into use under a deemer condition are subject to subsequent review and possible disapproval. Louisiana, Alabama and New York permit rate revisions based purely on a change in loss cost to be used immediately when filed. Otherwise the above provisions apply.

Bureau Made Rates

Insurers are required to become members of an authorized rating bureau. North Carolina now permits rates filed by the Bureau to be effective immediately upon filing (file and use); prior approval was previously required. Some deviation from Bureau rates is permitted for individual insurers. A uniform classification system is in effect.

State Made Rates

A state agency makes the rates and specifies rate classifications. All insurers must adhere to these rates. In Massachusetts, The Commissioner of Insurance sets rates for compulsory automobile insurance. In Texas, a State Board of Insurance promulgates the rate for automobile and various other forms of general insurance.

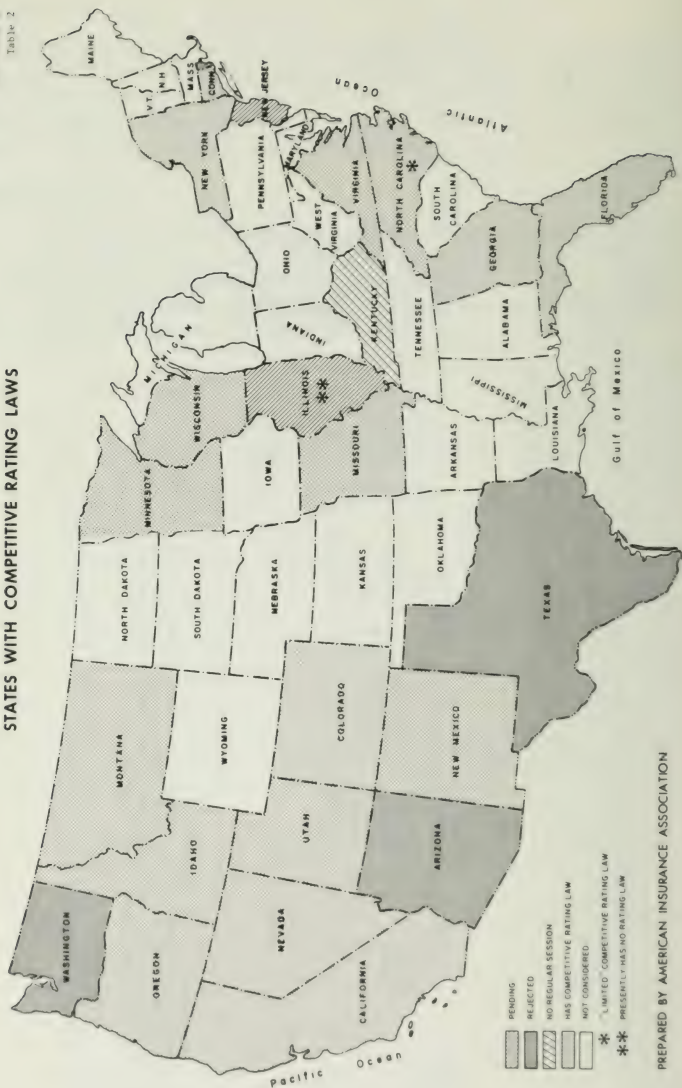
APPENDIX B
Table 1

No Rating Law	No Filing	Use and File	File and Use	Prior Approval	Bureau Made Rates	State Made Rates
Illinois* 5.4	California 11.1	New York(1) 6.8	Ohio 5.8	New York(1) 6.8	N. Carolina(3) 2.8	Texas 6.1
	Idaho 0.6	Florida 4.7	Michigan 4.9	Pennsylvania 6.4		Massachusetts (4) 2.7
	Georgia 2.6	Illinois 0.4	Indiana 2.4	New Jersey* 3.6		
	Virginia 2.4		Maine 0.5	Washington 1.9		
	Missouri 2.2	New Mexico 0.6	Delaware 0.3	Tennessee 1.9		
	Wisconsin 2.1	Utah 0.6	Wyoming 0.2	Alabama 1.8		
	Colorado 1.4	Nevada 0.2	Vermont(2) 0.2	Hawaii 0.5		
		D.C. 0.2		Kentucky 1.7		
				Rhode Is. 0.5		
				Connecticut 1.6		
				N.Hampshire 0.4		
				Louisiana 1.6		
				N. Dakota 0.3		
				Iowa 1.5		
				S. Dakota 0.3		
				Oklahoma 1.4		
				Maryland 0.3		
				Vermont(2) 0.2		
				S. Carolina 1.3		
				Arizona 1.1		
				Alaska 0.1		

- * A competitive rating law is pending.
- (1) A modified prior approval law is in effect for no-fault coverage, to expire Dec. 1978.
- (2) File and use, if increases do not exceed 10%.
- (3) As of 1-9-77, N. Carolina has a file and use law, but a rating bureau must prepare filing.
- (4) Compulsory no-fault; otherwise file and use.

517

STATES WITH COMPETITIVE RATING LAWS



PREPARED BY AMERICAN INSURANCE ASSOCIATION

APPENDIX C

Monitoring Competition: A Means Of Regulating The Property And Liability Business—N.A.I.C.—1974

(Extracts from a Study Prepared by the Staff of
the N.A.I.C. Central Office for Consideration by the N.A.I.C.)

TABLE 1

THE COMPETITIVE MARKET AS VIEWED BY THE ECONOMIST

The concepts needed for evaluating and monitoring competition in the property and liability insurance industry are also drawn from the economic theory of a competitive market.

The economic model of a competitive market rests on several assumptions. A competitive market is composed of numerous rational buyers and sellers, no one of which when operating alone can influence the market clearing price. The buyers and sellers interact in a market for a homogeneous product. Firms are free to enter and leave the market. Resources used in production must be relatively mobile. Consumers should be informed as to the terms being offered and producers should be aware of productive techniques used by other firms.

Supply in a competitive market is a function of the technical conditions of production, the price of input factors and the price of the goods in question. If any of these elements are altered, the quantity which a firm is willing to offer is changed. Demand in a competitive market is the aggregation of individual demands. Consumers, desiring to maximize their satisfaction, are willing to purchase varying quantities of goods at various prices. The price-quantity relationship reflects consumer tastes, prices of goods and services and consumer income.

The interaction between the supply and demand curves determines the price and quantity relationship which satisfies both the producer and the consumer. Every point on the supply curve gives the firm its profit maximizing quantity for every given price. Every point on the demand curve yields the quantity of goods which maximizes consumer satisfaction at a given price. Thus, the point where the supply and demand curves intersect determines the price and quantity producing joint satisfaction for both the consumers and the producers. Producing a different quantity or selling at a different price will generate pressures within the system to return to this equilibrium point. If prices are lower, the excess demand will induce increased supply. If prices are higher, the lessened demand will induce a reduction in supply. Competition, in the competitive model sense, implies a single uniform price which is the natural consequence of market forces.

Every economy must determine what to produce and how production is to be allocated. Our society seeks to maximize individual satisfaction. Productive efficiency is assured in the competitive model because of the ease of entry and exit of firms and a fixed output price which compels existing firms to produce at the point where average costs are minimum and the firms are earning no excess profits. Furthermore, distributional efficiency among consumers is assured. Therefore, in a competitive economy with established prices which no one individual can influence, no person can have his satisfaction increased without lessening that of another. If disequilibrium occurs, market forces automatically operate to restore the equilibrium. The market is impersonal, atomistic and democratic. It stresses individual preference. The price mechanism, in responding to surpluses and shortages, determines a single market clearing price and quantity. This price—quantity relationship is the best in the sense that it provides for efficient allocation and distribution of resources in such a manner that no individual economic unit could be made better off without harming another.

However, the model of perfect competition is unattainable for practical and possibly theoretical reasons. Furthermore, once any of the competitive assumptions are violated, the normative significance of the competitive model no longer holds. This, in turn, leads to a discussion of the concept of workable competition.

To judge the workability of competition in a given situation, one must examine (1) the performance of the market (2) the structure of the market, and (3) the conduct of the participants in the market. Each area must be examined individually and jointly and a determination made that no potential public policy measure exists that would lead to greater social gains than losses.

TABLE 2

ECONOMICS AND THE INSURANCE INDUSTRY

The tests of workable competition can be categorized as (1) structural indices; (2) performances indices; and (3) conduct.

1. Structure.

If the structure of a given market conforms closely to the assumptions underlying the competitive model, there is reasonable assurance that the market will tend to produce competitive results. The relevant structural indices include size and number of firms, ease of entry and exit, technical conditions of production, degree of product differentiation, and actual and potential growth of the market.

(a) In computing concentration ratios, care must be taken in determin-

ing the appropriate definitions of market, product, and the firm. This study concluded that market area should be defined in terms of the state, and product in terms of the annual statement lines of insurance. Company-group concentration ratios are deemed to be the most appropriate measures of concentration in examining the property and liability insurance markets. However, availability problems may make an examination of sub-state market areas useful.

In reviewing the literature, the preponderance of evidence points to the fact that the property and liability industry is unconcentrated. However, several recent studies indicate that the industry is not as unconcentrated as previous evidence suggested. The data collected by the authors of this study shows that concentration is increasing and, depending upon the definition of concentration, that some lines in some states exhibit a degree of concentration which might indicate oligopolistic structure. Data from a sample of prior approval and open competition states, however, demonstrates no significant difference in mean concentration between the two types of rating laws. Furthermore, no great difference in concentration emerges when measured on a sub-statewide or a territorial basis.

(b) In examining ease of entry, the capital cost seems small for a single line, one state company. However, a new multi-line, multi-state company faces substantial capital requirements. Also, the marketing entry costs of insurance can be substantial. Insurers electing to use the American agency system may be required to offer substantial commission inducements. Direct writers must gain product recognition through advertising campaigns or through the recruitment of a sales force. As might be expected in examining the creation of new companies and non-merger exits from the property and liability insurance industry, a direct relationship can be observed between the underwriting results in the industry and the number of new entries. As profitability improves, the number of entries increases; and, conversely, as underwriting experience deteriorates, the number of entries declines. In contrast, an examination of entries in prior approval states and open competition states, both for several years and just subsequent to the passage of an open rating law, leads to the conclusion that there is no difference exhibited between prior approval and open competition states.

(c) With respect to the technical conditions of supply and demand, the evidence to date on economies of scale in the property and liability insurance industry is incomplete. Additional research is needed in this area.

(d) No effort was made to quantify the amount of product differentiation which exists in property and liability insurance. However, the amount of advertising undertaken does not seem excessive when compared with other industries. It should be noted, however, that the existence of multiple prices for seemingly homogeneous products may have implications for product differentiation.

(e) Finally, the insurance industry is continuing to grow and expand.

The conclusions from this review of structure in the property and liability insurance business are somewhat ambiguous. It would appear that concentration in the property and liability insurance industry is not as great as in many industries. However, depending upon the type of definition of concentration one uses, there is evidence that elements of a concentrated structure exist. It also seems that, while entry is relatively easy, there are significant impediments to the formation of a nationwide all lines direct writing company. Therefore, our evidence concerning the structure of the property and liability insurance industry is inconclusive. The type of rating law utilized by a state does not seem to have a great impact upon the structure of the market in that state. In this regard, the fears of the opponents of open rating laws seem to be unfounded. The adoption of an open competition rating law does not seem to lead to an increased non-competitive structure.

2. Performance.

The second category of tests of workable competition relates to performance of the industry. If the market yields performance results comparable to those which would be expected from a competitive market, this is strong evidence that workable competition exists. Insurance regulators are interested in performance standards not only in the context of determining whether there is workable competition, so as to lessen the need for regulatory intervention, but also to implement such insurance regulatory goals as reasonable price, availability and solidity. This study reviewed the property and liability insurance business in the context of four performance tests; availability, profitability, price, and solvency.

(a) The willingness of the companies to make coverage available cannot be separated from the relative profitability of business. It should be noted that the period under consideration was one in which profits were improving. Therefore, quite aside from differences in rating laws, one would expect insurers to be more willing to write during these periods than in periods of declining profitability.

This study presented no independent evidence concerning availability. However, in reviewing the evidence of previous studies, the impact of open competition on availability of insurance reflects a mixed pattern. The record in California and Florida is quite good. Illinois reports some improvement. Evidence exists of improvement in New York although there has been a considerable increase in residual markets in that state (which might be accounted for by the adoption of a broader assigned risk program). The evidence in New York is unclear but judgment would seem to indicate that the open rating law has not yet had the effect upon the residual markets which was contemplated when the law was passed.

(b) Non-competitive elements may be present in a market if long-run

average profits exceed the amount necessary to attract and retain capital. None of the literature examined presented evidence of profits in open competition states exceeding profits in prior approval states. Using data developed by the authors of this study and a fairly rigorous statistical test, no evidence of different profit levels between open competition and prior approval states was discovered. This evidence is particularly strong since three substantially different sources of data and measurement techniques were utilized.

(c) Prices play a key role in economic theory. However, in examining a real-world situation, prices seldom reflect what one would expect from pure economic theory. This is particularly relevant for the insurance industry which reflects a situation in which an essentially homogeneous product is priced at widely divergent prices. Such a result might be due to real differentiations in the insurance product or service, or to lack of consumer knowledge concerning the alternatives. However, there exists no single dynamic theory of price behavior during a change from prior approval to open rating environments to which such results can be attributed with certainty. If prices are held at a level which yields excess profits, non-competitive elements may be present in the industry. In examining the evidence from a sample of prices of different insurance companies, no clear picture emerges. Using California as a standard of comparison, this study found no pattern of price levels, price variation, or frequency of price change which would distinguish prior approval from open competition rating. This, however, could be due to the elementary nature of the analysis undertaken. One conclusion, however, is that formal modeling of the dynamic behavior of insurance prices is an area for fruitful research.

(d) Solvency is an important performance standard in the insurance industry, especially because of the concern of some that competition would adversely affect solvency. Using data from the NAIC solvency test reports, no evidence of differences between solvency in prior approval and open competition states was found.

3. Conduct.

The third category of tests for workable competition is conduct. Under workable competition, firms are required to act independently. This implies an absence of cartels and other kinds of collusive behavior. These matters are extremely difficult to measure. They are usually carried on covertly, since most of this type of behavior is illegal. There is a fine line between behavior by a firm which indicates competition and behavior which may be predatory. Judgments concerning firm behavior must depend upon the facts in a given situation. As such, the area of conduct falls more within the realm of the lawyers and the courts than of economists.

Table 3

MONITORING THE EFFICACY OF COMPETITION AS A REGULATOR OF RATES

In determining the appropriate balance between the relative degree of regulation and competition, a basic point needs to be kept in mind. The stimulus for the move to open competition rating laws in the 1960's came more from dissatisfaction with the then-current system than from unquestioned confidence in competition. The move was more away from something, than toward something. In the minds of many, there has been an inadequate demonstration that insurance markets are sufficiently competitive to command public acceptance. Until this is done, open competition rating laws rest on a less than firm foundation. Unfortunately, the data upon which to evaluate the degree of competition is not readily available to the insurance regulator. To develop confidence in competition as the prime regulator of insurance rates, a system to measure and continuously monitor competition needs to be developed. Thus, adoption of the open competition laws creates a new set of ground rules requiring a new set of statistics and a carefully planned new machinery to collect, assemble and publish such data in a timely, organized, and meaningful fashion. A strong case can be made for incorporating, in new open competition laws—and for amending existing open competition laws—provisions for monitoring competition and for assessing the costs of the monitoring system against the insurers as a cost of doing business.

The administration of a monitoring system based upon the concept of workable competition consists of three elements; (1) economic surveillance, (2) enforcement and (3) monitoring underlying experience data.

1. Economic Surveillance.

Economic surveillance requires the collection, compilation, and analysis of data concerning the structure and performance of the insurance markets in the state so as to keep the commissioner informed on the effectiveness of competition. The type of information and possible method of its acquisition might be as follows.

a. Structural Tests. Concentration data could be developed by each individual state from the annual statements, by some computerized operation such as a private commercial firm or by the NAIC data base. However, if concentration information is needed for a market area smaller than statewide, it is not available in a consistent fashion from a central source. Departments currently possess information as to entry and exit of firms in their states. With respect to monitoring the degree and impact of economies of scale, there is little the regulator currently can do other than support in depth studies in this area. To monitor the degree of product differentiation,

the annual statement might be amended to incorporate advertising expenditures by line by state.

b. Performance Tests. Monitoring competition involves a continuing study of market (aggregate industry) performance as distinguished from a study of an individual company's performance. This will necessitate a significant reorientation in regulatory emphasis from that under prior approval laws. Overall industry availability of coverage, profitability, pricing activity, and solvency, not individual company figures, are the crucial concerns. To measure availability, information needs to be gathered concerning the residual markets, the distribution systems, underwriting, and the uninsured market. Much of this information can most readily be obtained by the individual insurance departments through current information gathering activities and questionnaires to producers and insurers. To obtain data on underwriting activity such as cancellations and renewals, the state could require the insurer to periodically report such information. With respect to profitability information, the NAIC adopted a uniform manner to compute profitability by line by state. After this program is implemented through the NAIC data base, it will be available automatically to every insurance department. At the present time, all states which require rate filings can obtain price information upon which price analysis can be made. The open competition states which do not require such filings may find it helpful to do so. As to solvency, each state is in possession of information concerning an insurer's financial condition as a part of its normal regulatory activity. In addition, the NAIC early warning system provides an additional tool to monitor this aspect of company performance.

The major purpose of the economic surveillance unit in an insurance department is to examine each of the indices of workable competition individually, interrelate the various indices, and make a judgment as to the existence or non-existence of workable competition in a given market. To the extent the information to monitor competition can best be collected by a single source rather than by each state individually, the cost of such a mechanism should be borne by the industry as a part of the cost of doing business and as a price for moving to open competition as it has so vigorously advocated.

2. Enforcement.

In addition to an economic surveillance unit a state implementing the open competition approach will need to perform the enforcement function. Illustrative enforcement activities include the following:

a. Reimpose prior approval if economic surveillance leads to the conclusion that there is an absence of workable competition.

b. Scrutinize industry conduct for illegal anticompetitive conduct (e.g. illegal concerted rate activity) and conduct any necessary investigations,

- c. Exercise appropriate action in a merger situation, and
- d. Examine insurers and statistical organizations for evidence of anti-competitive conduct.

3. Monitoring Underlying Experience.

An accelerated monitoring system for automobile insurance to provide experience data on a more timely basis was developed during the energy crisis under the auspices of the NAIC with the cooperation of the property and liability insurance industry. This system was designed to provide data on both a nationwide and a state by state basis. The data would include information on premiums, the number of claims, the amount of claims, etc. The implementation of such a system on a regular basis for those lines of insurance functioning under open competition would contribute to a more viable competitive market by (1) informing insurers on a more timely basis as to changes in underlying conditions so as to enable them to respond more quickly and (2) enabling regulators to ascertain whether insurers do respond to changing underlying conditions. On the one hand, if significantly improved experience does not lead to some rate reduction (in the absence of some countervailing explanation), this would lessen the likelihood of finding that workable competition exists. On the other hand, if the monitoring system reveals worsening experience, this would counter claims that a general pattern of increasing rates reflects an absence of competition. In the context of monitoring competition, regulation would be interested in experience data primarily on an aggregate, rather than individual company, basis (unless and until prior approval is reimposed).

To enhance the public credibility of the underlying experience data and to facilitate obtaining wanted data by the insurance regulator, a strong case can be made that the states should eliminate their dependence on company controlled organizations and compile such data through an independent organization, approved by the commissioner, which has no pecuniary interest in the results of the data compilation nor in the manner in which the data is used. As the energy crisis pointed up the need to Congress and the nation for developing better and publicly produced statistics, the accelerated monitoring system points up the need for better, more responsive, and continuous independent statistical data concerning the property and liability insurance business.

Appendix D
Sample Legislation
TABLE 1
COMPETITIVE RATING BILL

AN ACT to repeal and re-enact [refer to applicable sections of present rating law]; to regulate insurance rates; to provide for standards applicable to rates; to promote and encourage competition among insurers on a sound financial basis; to authorize and provide for examination and regulation of rate service and advisory organizations, and of joint underwriting and joint reinsurance organizations; to provide for the furnishing to the commissioner of rates and supplementary rate information; to provide for appellate review of actions by the commissioner; and to provide penalties.

Be it Enacted by the [insert appropriate reference to legislative bodies]:

SECTION 1: PURPOSES

The purposes of this Act are:

- (a) To promote the public welfare by regulating insurance rates to the end that they shall not be excessive, inadequate or unfairly discriminatory.
- (b) To encourage, as the most effective way to produce rates that conform to the standards of paragraph (a), independent action by and reasonable price competition among insurers.
- (c) To regulate cooperative action among insurers in the rate-making process in order to prevent practices that may tend to bring about monopoly or lessen or destroy competition.

SECTION 2: DEFINITIONS

In this Act, unless contrary to context:

- (1) "Supplementary rate information" includes any manual or plan of rates, statistical plan, classification, rating schedule, minimum premium, policy fee, rating rule, rate-related underwriting rule and any other information used by an insurer in making rates.
- (2) "Rate service organization" means any person other than a single insurer which assists insurers by compiling and furnishing loss or expense statistics and recommending, making or filing rates, forms or supplementary rate information.
- (3) "Advisory organization" means any person other than a single insurer which assists insurers or rate service organizations in the making of rates by compiling and furnishing loss or expense statistics or other statistical information and data, or by the submission of recommendations as to rates, forms or supplementary rate information.

- (4) The terms "rate service organization" and "advisory organization" shall not include a joint underwriting association, any actuarial or legal consultant, any employee of an insurer, or insurers under common control or management, or their employees, or manager.
- (5) "Inland marine insurance" shall be deemed to include insurance now or hereafter defined by statute, or by interpretation thereof, or if not so defined or interpreted, by ruling of the Insurance Commissioner, hereinafter referred to as commissioner, or as established by general custom of the business as inland marine insurance.

SECTION 3: SCOPE OF APPLICATION*

The provisions of this Act shall apply to all insurance on risks or on operations in this State, except:

- (1) Reinsurance, other than joint reinsurance to the extent stated in Section 12 of this Act;
- (2) Any policy of insurance against loss or damage to or legal liability in connection with property located outside this State, or any motor vehicle or aircraft principally garaged and used outside of this State, or any activity wholly carried on outside this State;
- (3) Insurance of vessels or craft, their cargoes, marine builders' risks, marine protection and indemnity, or other risks commonly insured under marine, as distinguished from inland marine insurance policies;
- (4) Accident, health, or life insurance;
- (5) Annuities;
- (6) Title insurance;
- (7) Mortgage guaranty insurance; and
- (8) Workers' compensation and employer's liability insurance written in connection therewith.

The provisions of this Act shall not apply to hospital service or medical service corporations, investment companies, mutual benefit associations, or fraternal beneficiary associations.

SECTION 4: RATE STANDARDS

(1) General

Rates shall not be excessive, inadequate or unfairly discriminatory, nor shall an insurer charge any rate which if continued will have or tend to have the effect of destroying competition or creating a monopoly.

**Note:* This section should be adapted to the language and definitions used in the applicable state insurance law.

(2) Excessiveness

(a) Competitive Market

Rates are not excessive if a reasonable degree of price competition exists at the consumer level with respect to the class of business to which they apply. A reasonable degree of price competition in a given class of business shall be presumed to exist if insurers are actively engaged in the class of business in this state and there are rate differentials.

(b) Non-competitive Market

If such competition does not exist, rates are excessive if they are likely to produce a long-run underwriting profit that is unreasonably high for the class of business, or if expenses are unreasonably high in relation to the services rendered.

(3) Inadequacy

Rates are inadequate if they are clearly insufficient to sustain projected losses and expenses in the class of business to which they apply.

(4) Unfair Discrimination

A rate is not unfairly discriminatory in relation to another in the same class if it reflects equitably the differences in expected losses and expenses. Rates are not unfairly discriminatory because different premiums result for policyholders with like loss exposures but different expense factors, or like expense factors but different loss exposures, so long as the rates reflect the differences with reasonable accuracy. Rates are not unfairly discriminatory if they are averaged broadly among persons insured under a group, franchise or blanket policy.

SECTION 5: RATING METHODS

In making rates, the following criteria shall be applied:

(1) Basic Factors in Rates

Due consideration shall be given to past and prospective loss and expense experience within and outside this State, to catastrophe hazards, to a reasonable margin for underwriting profit and contingencies, to investment income from unearned premium and loss reserves, to trends within and outside this State, to dividends or savings to be allowed or returned by insurers to their policyholders, members or subscribers, and to all other factors, including judgment factors.

(2) Classification

Risks may be classified in any reasonable way for the establishment of rates and minimum premiums, except that classifications may not be based on race, colour, creed or national origin. Rates thus produced may be modified for individual risks in accordance with rating plans or schedules which establish reasonable standards for measuring probable variations in hazards, expenses, or both.

(3) Expenses

The expense provisions included in the rates to be used by an insurer may reflect the operating methods of the insurer and, so far as it is credible, its own expense experience.

SECTION 6: FILING OR RATES

- (1) Except as to inland marine risks which by general custom of the business are not written according to manual rates and rating plans, every authorized insurer and every rate service organization which has been designated by any insurer for the filing of rates under Section 8(2) shall file with the commissioner all rates and supplementary rate information and all changes and amendments thereof made by it for use in this State within 30 days after they become effective.
- (2) The commissioner may require the filing of supporting data including:
 - (a) The experience and judgment of the filer, and, to the extent it wishes or the commissioner requests, of other insurers or rate service organizations;
 - (b) The filer's interpretation of any statistical data relied upon; and
 - (c) A description of the methods used in making the rates.
- (3) Upon written consent of the insured, stating his reasons therefore, a rate in excess of that provided by an otherwise applicable filing may be used on a specific risk, provided that such rate is filed with the commissioner in accordance with subdivision (1) of this section.

SECTION 7: FILINGS OPEN TO INSPECTION

Each filing and supporting information filed under this Act shall, as soon as filed, be open to public inspection at any reasonable time. Copies may be obtained by any person on request and upon payment of a reasonable charge thereof.

SECTION 8: DELEGATION OF RATEMAKING AND RATE FILING OBLIGATIONS

(1) Ratemaking

An insurer may establish rates and supplementary rate information based on the factors in Section 5, using if desired the recommendations of an advisory organization, or it may use rates and supplementary rate information prepared by a rate service organization, with average expense factors determined by the rate service organization or with such modification for its own expense and loss experience as the credibility of that experience allows.

(2) Rate Filing

An insurer may discharge its obligation under Section 6 by giving notice to the commissioner that it uses rates and supplementary rate in-

formation prepared by a designated rate service organization, with such information about modifications thereof as are necessary to inform the commissioner. The insurer's rates and supplementary rate information shall be those filed from time to time by the rate service organization, including any amendments thereto as filed, subject, however, to the modifications filed by the insurer.

(3) Exchange of Information

Licensed rate service organizations, advisory organizations, and admitted insurers are authorized to exchange information and experience data with rate service organizations, advisory organizations, and insurers in this and other states and may consult with them respect to ratemaking.

SECTION 9: DISAPPROVAL OF RATES

If the commissioner finds after a hearing that a rate is not in compliance with Section 4, he shall issue an order specifying in what respects it so fails, and stating when, within a reasonable period thereafter, such rate shall be deemed no longer effective. Said order shall not affect any contract or policy made or issued prior to the expiration of the period set forth in said order.

SECTION 10: RATE SERVICE ORGANIZATIONS

- (1) No rate service organization shall provide any service relating to the rates of any insurance subject to this Act, and no insurer shall utilize the service of such organization for such purposes unless the organization has obtained a licence from the commissioner.
- (2) No rate service organization shall refuse to supply any services for which it is licenced in this State to any insurer authorized to do business in this State and offering to pay the fair and usual compensation for the services.
- (3) A rate service organization applying for a licence shall include with its application:
 - (a) A copy of its constitution, charter, articles of organization, agreements, association or incorporation, and a copy of its by-laws and any other rules or regulations governing its activities;
 - (b) A list of its members and subscribers;
 - (c) The name and address of one or more residents of this State upon whom notices, process affecting it or orders of the commissioner may be served; and
 - (d) A statement showing its technical qualifications for acting in the capacity for which it seeks a licence.
- (4) If the commissioner finds that the applicant and the natural persons through whom it acts are qualified to provide the services proposed, and that all requirements of law are met, he shall issue a licence specifying

the authorized activity of the applicant. He shall not issue a licence if the proposed activity should tend to create a monopoly or to lessen or to destroy price competition. Licences issued pursuant to this section shall remain in effect until the licensee withdraws from the state or until the licence is suspended or revoked.

- (5) Any amendment to a document filed under this section shall be filed promptly. Failure to file any such amendment shall be a ground for suspension of the licence during the period of non-compliance. Willful or repeated failures to file such amendments shall be a ground for revocation of the licence.
- (6) Every rating organization providing services in this State on the effective date of this Act, may continue to provide services thereafter as a rate service organization, subject to the provisions of this Act, pending its application to the commissioner, to be made within 30 days after the effective date of this Act, for a licence to provide services as a rate service organization.

SECTION 11: ADVISORY ORGANIZATIONS

No advisory organization shall conduct its operations in this State unless and until it has filed with the commissioner: (a) a copy of its constitution, charter, articles of organization, agreement, association or incorporation, and a copy of its by-laws, and any other rules or regulations governing its activities, (b) a list of its members and subscribers, and (c) the name and address of one or more residents of this State upon whom notices, process affecting it or orders of the commissioner may be served. Any amendments to a document filed under this section shall be filed promptly.

SECTION 12: JOINT UNDERWRITING AND JOINT REINSURANCE ORGANIZATIONS

- (1) Every group, association or other organizations of insurers which engages in joint underwriting or joint reinsurance through such group, association or organization or by standing agreement among the members thereof shall file with the commissioner: (a) a copy of its constitution, articles of association and by-laws, (b) a list of its members, and (c) the name and address of a resident of this State upon whom notices or orders of the commissioner or process may be served. Every such group, association or other organization shall notify the commissioner promptly if any change in the documents required to be filed with him.
- (2) If after a hearing, the commissioner finds that any activity or practice of any such group, association or other organization is inconsistent with the provisions of this Act, he may issue a written order specifying the inconsistencies and requiring the discontinuance of such activity or practice.

SECTION 13: RATE AGREEMENTS AMONG INSURERS PROHIBITED

- (1) Except with respect to apportionment agreements among insurers approved by the commissioner pursuant to Section 16, no insurer shall assume any obligation to any person, other than a policyholder or other insurers which with it are under common control or management or are members of a joint underwriting or joint reinsurance organization, to use or adhere to certain rates or rules, and no other person shall impose any penalty or other adverse consequence for failure of an insurer to adhere to certain rates or rules.
- (2) Members and subscribers of rate service organizations or advisory organizations may use the work products and services of such organizations as their individual judgment may dictate. Such use by two or more authorized insurers shall not be sufficient to support a finding that an agreement to adhere exists and may be used only for the purpose of supplementing direct evidence of such an agreement.

SECTION 14: RECORDING AND REPORTING OF EXPERIENCE

The commissioner shall promulgate or approve reasonable rules, including rules providing statistical plans, for use thereafter by all insurers in the recording and reporting of loss and expense experience, in order that the experience of such insurers may be made available to him. No insurer shall be required to record or report its experience on a classification basis inconsistent with its own rating system. An insurer may at its election report its experience to any rate service organization or advisory organization with which it affiliates.

SECTION 15: EXAMINATION OF RATE SERVICE ORGANIZATIONS AND JOINT UNDERWRITING AND JOINT REINSURANCE ORGANIZATIONS

The commissioner shall, at least once in 5 years, make or cause to be made an examination of each rate service organization, and he may, as often as he may deem expedient, make or cause to be made an examination of each advisory organization under Section 11 and of each group, association, or other organization referred to in Section 12. Such examination shall only relate to the activities conducted pursuant to this Act. The reasonable costs of any such examination shall be paid by the organization examined upon presentation to it of a detailed account of such costs. The officers, managers, agents and employees of any such organization may be examined at any time under oath and shall exhibit all books, records, accounts, documents or agreements governing its method of operation. In lieu of any such examination, the commissioner may accept the report of an examination made by the insurance supervisory official of another State, pursuant to the laws of such State.

SECTION 16: APPORTIONMENT AGREEMENTS AMONG INSURERS

Agreements may be made among insurers with respect to equitable apportionment among them of insurance which may be afforded applicants who are in good faith entitled to but who are unable to procure such insurance through ordinary methods and such insurers may agree among themselves on the use of reasonable rate modifications for such insurance, such agreements and rate modifications to be subject to the approval of the commissioner.

SECTION 17: HEARING AND JUDICIAL REVIEW

Any insurer, rate service organization or advisory organization to which the commissioner has directed an order or decision made without a hearing may, within thirty days after notice to it of the order or decision, make written request to the commissioner for a hearing thereon. The commissioner shall hear such party or parties within twenty days after receipt of such request and shall give not less than ten days' written notice of the time and place of the hearing. Within fifteen days after such hearing the commissioner shall affirm, reverse or modify his previous action, specifying his reasons therefor. Pending such hearing and decision thereon the commissioner may suspend or postpone the effective date of his previous action. Any order or decision of the commissioner shall be subject to review by the [_____] Court.

SECTION 18: PENALTIES

The commissioner may, if he finds that any person or organization has violated any provision of this Act, impose a penalty of not more than fifty dollars (\$50) for each such violation, but if he finds such violation to be willful he may impose a penalty of not more than five hundred dollars (\$500) for each such violation. Such penalties, which may not in the aggregate exceed \$_____, may be in addition to any other penalty provided by law.

The commissioner may suspend the licence of any rate service organization or insurer which fails to comply with an order of the commissioner within the time limited by such order, or any extension thereof which the commissioner may grant. The commissioner shall not suspend the licence of any rate service organization or insurer for failure to comply with an order until the time prescribed for an appeal therefrom has expired, or if an appeal has been taken, until such order has been affirmed. The commissioner may determine when a suspension of a licence shall become effective and it shall remain in effect for the period fixed by him, unless he modifies or rescinds such suspension, or until the order upon which such suspension is based is modified, rescinded or reversed.

No penalty shall be imposed and no licence shall be suspended or revoked except upon a written order of the commissioner, stating his findings, made after a hearing held upon not less than ten days' written notice to such person or organization specifying the alleged violation.

SECTION 19: POLICY FORMS

Except for fidelity, surety or guaranty bonds and except as to inland marine risks which by general custom of the business are not written according to manual rates or rating plans, no policy form applying to insurance on risks or operations covered by this Act shall be delivered or issued for delivery unless it has been filed with the commissioner and either he has approved it, or 30 days have elapsed and he has not disapproved it as ambiguous, misleading, or deceptive.

SECTION 20: EXISTING RATES, SUPPLEMENTARY RATE INFORMATION AND POLICY FORMS

Rates, supplementary rate information and policy forms lawfully in use on the effective date of this Act may be continued to be used thereafter, unless subsequently disapproved after a hearing.

SECTION 21: PAYMENT OF DIVIDENDS

Nothing in this Act shall be construed to prohibit or regulate the payment of dividends, savings, or unabsorbed premiums deposits allowed or returned by insurers to their policyholders, members or subscribers. A plan for the payment of dividends, savings, or unabsorbed premium deposits allowed or returned by insurers to their policyholders, members or subscribers shall not be deemed a rating plan or system.

SECTION 22: CONFLICTING STATUTES

All other statutes in conflict with this Act are hereby repealed.

SECTION 23: EFFECTIVE DATE

This Act shall take effect _____.

November 23, 1976.

TABLE 2

EXTRACTS FROM THE INSURANCE ACT OF ALBERTA

Alberta
Automobile
Insurance
Board

321.1(1) The Lieutenant Governor in Council may establish a board to be known as the "Alberta Automobile Insurance Board" (hereafter called "the Board") consisting of such members as the Lieutenant Governor in Council appoints.

(2) The Lieutenant Governor in Council may

- (a) designate one of the members of the Board as chairman and another as vice-chairman, and
- (b) fix the remuneration and provide for the payment of expenses to be paid to the members who are not employees of the Government.

(3) In accordance with The Public Service Act there may be appointed such staff and other persons as may be required by the Board.

(4) Subject to the approval of the Lieutenant Governor in Council, the Board may from time to time appoint one or more experts or persons having special technical or other knowledge to inquire into and report to the Board in respect of any matter before the Board or in respect of which the Board deems it necessary to have information for the proper carrying out of its duties.

(5) A person appointed by the Board pursuant to subsection (4) shall be paid such remuneration as may be prescribed by the Lieutenant Governor in Council.

(6) A majority of members constitute a quorum of the Board for the purpose of exercising its powers and performing its duties.

(7) An order, direction, approval or other instrument that the Board is permitted or required to make, may be made on its behalf by the chairman, vice-chairman or any other member of the Board.

(8) An order, direction, approval or other instrument purporting to be signed by the chairman, vice-chairman or a member of the Board on behalf of the Board shall be admitted in evidence in any proceedings as prima facie proof

- (a) that the order, direction, approval or instrument is the act of the Board or a quorum thereof, and
- (b) that the person signing it was authorized to do so without proof of the appointment of the person signing as a

member of the Board, or his designation as chairman or vice-chairman, as the case may be, or of his signature.

(9) The Board may make rules governing its procedures.

(10) The chairman, vice-chairman and every other member of the Board has the power of a commissioner under the Public Inquiries Act. New, 1971, c. 58, s. 8

321.2(1) In this section and sections 321.3, 321.4, 321.5 and 321.6 "minimum insurance" means the insurance referred to in section 300, subsection (1) and section 300.1 and in the regulations made pursuant to section 300.2.

Minimum
Insurance

(2) The Board has the power

(a) to investigate any matter it thinks fit respecting automobile insurance in Alberta, including rates, benefits and availability of automobile insurance, and

(b) to prohibit

(i) any rate being charged by an insurer for the minimum insurance above a rate filed pursuant to section 321.4, or

(ii) any change in class of a vehicle from the classification of that vehicle filed pursuant to section 321.4, or

(iii) any change which would have the effect of increasing a rate for the minimum insurance for any insured person or class of insured persons, or which would have the effect of changing a vehicle from one class to another,

unless the increase or change has first been approved (or neither approved nor prohibited) by the Board under section 321.4.

New, 1971, c. 53, s. 8; 1972, c. 55, s. 6.

321.3(1) In this section and sections 321.2, 321.4, 321.5 and 321.6 "rates" means the price charged for a motor vehicle liability policy or any coverage under that policy.

Rates

(2) On or before July 1, 1971 every insurer of automobiles shall file with

(a) the Board, or

(b) if the Board has not been established, the Superintendent,

its full schedule of rates in effect in Alberta on April 1, 1971 applicable to every motor vehicle liability insurance policy issued

by the insurer showing separately the rates charged for the minimum insurance, (if any).

(3) Every insurer not licensed on April 1, 1971 but licensed thereafter, shall file with the Board its full schedule of rates it intends shall be applicable to every motor vehicle liability insurance policy to be issued by it in Alberta showing separately

- (a) the number and types of classes of vehicles proposed to be insured by the insurer in respect of which the minimum insurance applies, and
- (b) the rates proposed to be charged for the minimum insurance with respect to each class of vehicles.

(4) Upon the establishment of the Board, the Superintendent shall send all the particulars filed with him pursuant to subsection (2) to the Board. New, 1971, c. 53, s. 8

Approval
of rates

321.4 (1) On or before January 1, 1972, or such later date as the Minister may allow, every insurer shall file with the Board the rates it proposes to charge for the minimum insurance in Alberta on and after April 1, 1972, whether or not the rates are included in the rates filed under section 321.3, subsection (2).

(2) On and after April 1, 1972 no insurer shall

- (a) charge the proposed rates filed under subsection (1) or the proposed rates filed under section 321.3, subsection (3) or any other rate for the minimum insurance, or
- (b) change a vehicle from one class to another or add to or in any manner change the number or type of classes of vehicles filed with the Board prior to April 1, 1972,

unless

(c) the Board has approved

- (i) the rates,
- (ii) the classification of vehicles, and
- (iii) the rates attaching to each class of vehicle,

or

(d) the rates, classification of vehicles and the rates attaching to each class of vehicle have been filed with the Board for 60 days and the Board has neither approved nor disapproved the filing or any part thereof.

(3) Where an insurer receives an approval or is permitted to proceed pursuant to subsection (2), the insurer shall not

- (a) increase its rates with respect to the minimum insurance

- either generally or with respect to a particular class of vehicle, or
- (b) change the class of any vehicle with respect to the minimum insurance, or
- (c) make any other change which would have the effect of increasing any rate for the minimum insurance or changing any class of any vehicle with respect to the minimum insurance,

without first applying to the Board and receiving its approval pursuant to subsection (5) or subsection (6).

(4) Where the Board is not satisfied that an insurer has filed all the matters referred to in this section, or requires additional details or information, it may, by order directed to the insurer, require the additional information and details.

- (5) Where an insurer wishes to
 - (a) increase any rate for the minimum insurance, or
 - (b) change the class of any vehicle or the number or types of classes of vehicles, or
 - (c) change any rate attaching to any particular class of vehicle, or
 - (d) make any other change which would have the effect of increasing any rate for the minimum insurance or any change which would have the effect of changing the number or type of class of vehicles with respect to the minimum insurance,

it may apply to the Board for approval of the increase, change of class or classification or the number or type thereof or any other change and the Board in its discretion by order may

- (e) approve the application or any part thereof, or
- (f) prohibit the application or part thereof.

(6) Where an insurer makes an application to the Board pursuant to subsection (5) and the application has not been approved or prohibited during a period of 60 days from the date the application is filed, the application shall be deemed to have been approved and the increase in rates, change of class or classification of vehicle or the type or number thereof or any other change applied for pursuant to subsection (5) may be made by the insurer upon expiration of the 60-day period.

(7) Where an application by an insurer has been approved pursuant to this section, the Board may at any time thereafter investigate

- (a) the rates of the insurer for the minimum insurance, or
- (b) the division into classes of vehicles and the classification of vehicles and the number and type thereof with respect to the minimum insurance, or
- (c) the rates for the minimum insurance attaching to any particular class of vehicles,

and notwithstanding any prior approval, may order the insurer to reduce or change its rates, to change the classification of any vehicle or the class or number or type of vehicles or make any other change with respect to the minimum insurance in the manner directed by the Board. New, 1971, c. 53, s. 8

321.5 (1) An insurer who

- (a) fails to file its rates, pursuant to section 321.3, subsection (2) or section 321.3, subsection (3), or
- (b) fails to file the rate it proposes to charge pursuant to section 321.4, subsection (1), or
- (c) charges the proposed rate prior to its approval contrary to section 321.4, subsection (2), or
- (d) increases the rate payable for the minimum insurance contrary to section 321.4, subsection (3), or
- (d1) adds to or in any manner changes the class of vehicles, the classification of a vehicle or the number or type thereof contrary to section 321.4, subsection (3), or
- (d2) makes any change in a rate or class or classification of vehicles without approval pursuant to section 321.4, subsections (5) and (6), or
- (e) in any manner fails to comply with an order or direction of the Board, or
- (f) fails to comply with the regulations

is guilty of an offence and liable on summary conviction to a fine of not more than \$5000.

(2) Where an insurer is convicted of a second or subsequent offence under this section the Minister may suspend the licence of the insurer.

(3) Where the Minister suspends the licence of an insurer the Minister shall report the suspension to the Lieutenant Governor in Council who may

- (a) remove the suspension with or without conditions, or
- (b) confirm the suspension for a stated time or until such conditions as he may impose have been met, or both, or
- (c) terminate the licence. New, 1971, c. 53, s. 8

321.6 (1) The Lieutenant Governor in Council may make regulations

- (a) establishing a plan for the equitable assignment of risks and empower the Board to direct an insurer to accept an assignment of risk, and
- (b) to permit rating bureaus to file on behalf of one or more insurers, schedules of rates or an application for an increase in rates for the minimum insurance.

(2) Regulations made under subsection (1), clause (b) do not relieve an insurer on whose behalf a rating bureau is acting from ensuring that the provisions of this Part relating to filing and the matters required by sections 321.3 and 321.4 are complied with.

New, 1971, c. 53, s. 8

321.7 (1) The Board shall make and submit to the Minister an annual report on the operation of the Board.

Annual
report

(2) The Minister shall lay the report before the Legislative Assembly if it is then in session or if it is not, within 15 days of the opening of the next following session.

New, 1971, c. 53, s. 8

321.8 (1) Except as provided in this section

Appeal

- (a) every decision, order, approval, regulation, direction or proceeding of the Board is final, and
- (b) no decision, order, approval, regulation, direction or proceeding of the Board shall be questioned or reviewed, restrained or removed by prohibition, injunction, certiorari or any other process or proceeding in any court.

(2) Upon a question of jurisdiction or upon a question of law, an appeal lies from the Board to the Appellate Division of the Supreme Court of Alberta.

(3) Leave to appeal shall be obtained from a judge of the court of appeal upon application made within one month after the making of the decision, order, approval, regulation, direction or proceeding sought to be appealed from, or within such further time as the judge under special circumstances may allow and upon notice to the parties and to the Board and upon hearing such of them as appear and desire to be heard and the costs of the application are in the discretion of the judge.

New, 1971, c. 53, s. 8

321.9 (1) Nothing in sections 321.2, 321.3 or 321.4 prevents an insurer from charging a reduced rate for the minimum insurance

Reduced
rate

- (a) where a person owns two or more vehicles classified for the minimum insurance under the same or a different class, or
- (b) where a person owns two or more vehicles under two or more policies with the same insurer.

(2) Notwithstanding subsection (1), where an insurer charges a reduced rate for the minimum insurance, he shall not increase the rate unless the increased is approved (or neither approved nor prohibited) pursuant to section 321.4, subsection (5) or (6).

New, 1972, c. 55, s. 12.

APPENDIX E

The Early Warning System N.A.I.C. Regulatory Tests for Property and Liability Insurers

(Extracted from "Using the Early Warning System"
by the National Association of Insurance Commissioners—1976)

I. HOW THE EARLY WARNING SYSTEM WORKS

The N.A.I.C. Early Warning System, developed by a committee of state insurance regulators, is intended to assist the various state insurance departments in identifying property and liability insurance companies requiring particularly close surveillance. The system is based on eleven ratios, or tests, which have been shown to be effective in distinguishing between financially troubled and sound companies.

Purposes of the System

The purposes of the Early Warning System are to help state insurance department personnel quickly identify companies requiring close surveillance and determine the form that surveillance should take. The system is not intended to replace in-depth financial analysis or on-site examination of companies. It can, however, provide a guide to those companies for which deeper analysis may be required. It can also serve as an aid in determining which companies may require special on-site examinations, either to resolve specific issues or to verify overall financial solidity.

Although the system has been shown to be effective in distinguishing between troubled and sound companies (as discussed below), it is by no means foolproof. This fact has four important implications:

1. No state should rely completely on the Early Warning System as its only form of surveillance.
2. Important decisions—such as licencing decisions—should not be based on test results without further analysis and examination of the company concerned.
3. Because these tests are easily subjected to possible misinterpretation and misuse, any valid interpretation of test data must depend to a considerable extent on the judgment of knowledgeable and experienced reviewers.
4. The results of individual early warning tests for each company should be carefully analyzed. If areas of concern are identified, a review of that company's annual statement or other inquiries should be made to determine whether an examination is required.

Selection of Priority Companies

By comparing test results for all companies with the results for companies becoming insolvent during recent years, a "usual range" of test results has been determined for each of the individual audit ratios. By "usual" is meant not only the range in which most companies normally fall, but also the range in which the value of the ratio falls in a normal year.

Accordingly, when a fundamental variable (such as surplus) is significantly disturbed by economic forces (a drop in the stock market) many of the calculated values will fail to fall in their normal or "usual range".

Nationwide, about 15 percent of the companies tested are expected to receive a priority company designation. This designation is assigned to each insurer which has four or more test results outside the usual range. Priority companies are the companies most likely to require closer than usual monitoring by the insurance department. Their test results should be verified, and further analysis of their annual statements should be performed to determine whether an on-site examination is called for.

Although the intent of the priority company system is to assist insurance department personnel in focusing their immediate attention on those companies most likely to be experiencing financial difficulty, not all the priority companies will necessarily be troubled. Some may have taken action to eliminate weaknesses that became apparent during the prior year. It is also possible that unusual accounting methods may make test results appear less favourable than is warranted, or that errors may occur in calculating test results. However, unless a given priority company is known to be financially sound, careful analysis and examination of that company would be appropriate.

Non-priority companies are less likely to require in-depth review or on-site examination. However, the fact that a company is not given the priority classification by the Early Warning System should not be taken as a guarantee of continuing financial solidity. The results of individual tests for each non-priority company should be carefully analyzed. If areas of concern are identified, a review of the company's annual statement should be made to determine whether an examination is required.

Regulatory Test Reports

Each state will be provided with two types of reports from the Early Warning System:

1. Preliminary Releases
2. Final Release

Preliminary Releases

Periodically, as test results become available, each state will receive Preliminary Releases. The first release is included in this binder, under the tab "Preliminary Releases". Future releases should be inserted under this tab as they are received.

The purpose of these Preliminary Releases is to provide an overview of test results for all companies and to identify the priority companies. In each Preliminary Release, there are two reports: one prepared in descending order according to the number of exceptional test values for each company, the other is prepared in company name order. Test results falling outside the usual range are indicated by an asterisk.

Final Release

When the test results for substantially all of the companies have been calculated each year, a final release will be issued. The purpose of this report is to provide a reference containing test results for all companies and groups or fleets. The final release will include all companies (whether test results are available or not) in the same format as the preliminary releases. If test results are not available for a company, a statement will explain the reason for the omission. Priority companies are identified by a "P" before the company name. Amended statements when provided by an insurer are indicated by an "A" before the company name. A revised report for an insurer which has been included in a previous report is identified by an "R".

II. THE REGULATORY TESTS

This chapter describes the eleven regulatory tests and provides suggestions for interpreting test results and determining the types of further analysis needed. The test fall into four groups:

- Overall Tests
- Profitability Tests
- Liquidity Tests
- Reserve Tests

The tests are as follows:

Test 1: Premium to Surplus (Overall)

A company's surplus provides a cushion for absorbing above-average losses. The premium to surplus ratio measures the adequacy of this cushion. The higher the ratio, the more risk the company bears in relation to the surplus available to absorb loss variations . . . The usual range for the premium to surplus test is up to 300%.

Test 2: Change in Underwritings (Overall)

Major increases or decreases in net premiums written indicate a lack of stability in the company's operations. A major increase in premium may signal abrupt entry into new lines of business or sales territories. In addition, such an increase in writings may be a sign that the company is increasing cash inflow in order to meet loss payments. . . . The usual range for the change in writing tests is from an increase of 33% to a decrease of 33%.

Test 3: Surplus Aid to Surplus (Overall)

The use of surplus aid reinsurance treaties may be taken as an indication that company management believes surplus to be inadequate. In addition, the continued solvency of companies with a large portion of surplus deriving from surplus aid may depend upon the continuing cooperation of the reinsurer. . . . The usual range for the ratio of surplus aid to surplus is less than 25%.

Test 4: Two Year Adjusted Underwriting Ratio (Profitability)

The adjusted underwriting ratio is a measure of the underwriting profitability of an insurance company. Over the long run, the profitability of the business is a principal determinant of the company's financial solidity and solvency. . . . The usual range for the two year adjusted underwriting ratio is less than 110%.

Test 5: Investment Yield (Profitability)

In addition to measuring one important element in profitability, the investment yield test also provides an indication of the general quality of the company's investment portfolio. . . . The usual range for investment yield is between 9.9 and 4.0%.

Test 6: Change in Surplus (Profitability)

The change in surplus is, in a sense, the ultimate measure of the improvement or deterioration in the company's financial condition during the year. . . . The usual range for the change in surplus test is from minus 10% to plus 50%.

Test 7: Liabilities to Liquid Assets (Liquidity)

The ratio of liabilities to liquid assets is a measure of the company's ability to meet the financial demands that may be placed upon it. It also provides a rough indication of the possible implications for policyholders if liquidation becomes necessary. . . . The usual range for the liabilities to liquid assets ratio is below 105%.

Test 8: Agent's Balances to Surplus (Liquidity)

The ratio of agent's balances to surplus measures the degree to which solvency depends upon an asset which frequently cannot be realized in the event of liquidation. In addition, the ratio is reasonably effective in distinguishing troubled from sound companies. . . . The usual range for the agent's balances to surplus ratio is less than 40%.

Test 9: One Year Reserve Development to Surplus (Reserve)

In addition to measuring the accuracy with which reserves were established one year ago, the ratio of one-year reserve development to surplus provides an indirect indication of management's opinion of the adequacy of surplus. Unless surplus is felt to be low, management frequently tends to over-estimate reserves, for income tax and other reasons. . . . The usual range for the ratio of one year reserve development to surplus is less than 25%.

Test 10: Two Year Reserve Development to Surplus (Reserve)

The usual range for the two year test is also less than 25%.

Test 11: Estimated Current Reserve Deficiency to Surplus (Reserve)

The estimated current reserve deficiency or redundancy is taken as a percentage to surplus. This estimated deficiency is the difference between the estimated reserves required by the company and the actual reserves maintained. . . . The usual range for the ratio . . . is less than 25%.

APPENDIX F

The Insurance Act Revised Statutes of Ontario, 1970 Sections 365-367 Pertaining to Rate Regulation

365. DISCRIMINATION IN RATES

- (1) No rating bureau and no insurer authorized to transact the business of insurance in Ontario shall fix or make a schedule of rates or charge a rate that discriminates unfairly between risks in Ontario of essentially the same physical hazards in the same territorial classification, or if the rate is a fire insurance rate, that discriminates unfairly between risks in the application of like charges or credits or that discriminates unfairly between risks of essentially the same physical hazards in the same territorial classification and having substantially the same degree of protection against fire.

Commencement of Section

- (2) This section does not come into force until a day to be named by the Lieutenant Governor by his proclamation. R.S.O. 1970, c. 224, s. 365.

366. AUTHORITY TO REQUIRE INFORMATION TO BE FILED

- (1) The Superintendent may, on written complaint by an insurer or an insured that discrimination exists or upon such information filed with him as the Superintendent considers sufficient to justify an investigation, give notice in writing to a rating bureau or insurer, requiring such rating bureau or insurer to file with the Superintendent any schedules of rates or particulars showing how any specific rate is made up and any other information that he may require.

Time Limit for Filing Information

- (2) Such rating bureau or insurer shall, within five days after the receipt of the notice, file with the Superintendent the schedules, particulars and other information required.

Issue of Order Prohibiting Rate

- (3) The Superintendent may, within thirty days after the receipt of the notice, file with the Superintendent the schedules, particulars and other information required.

Notice of Order

- (4) The Superintendent shall forthwith deliver to the rating bureau or insurer a copy of such order and reasons therefor and shall cause notice thereof to be published forthwith in The Ontario Gazette.

Rating Bureau not to Increase Rates

- (5) No rating bureau or insurer shall remove such discrimination by increasing the rates on any risk or class of risks affected by such order unless it be made to appear to the satisfaction of the Superintendent that such increase is justifiable.

Offence

- (7) A rating bureau, insurer or other person failing to comply with such order is guilty of an offence.

Appeal

- (8) This section does not come into force until a day to be named by the Lieutenant Governor by his proclamation. R.S.O. 1970, c. 224, s. 366.

367. SUPERINTENDENT EMPOWERED TO ORDER RATE ADJUSTMENT

- (1) It is the duty of the Superintendent, after due notice and a hearing before him, to order an adjustment of the rates for automobile insurance whenever it is found by him that any such rates are excessive, inadequate, unfairly discriminatory or otherwise unreasonable.

Appeal from Order

- (2) An order made under this section does not take effect for a period of ten days after its date, and is subject to appeal within that time by any insured, insurer or rating bureau, in the manner provided by section 11 and, in the event of an appeal, the order of the Superintendent does not take effect pending the disposition of the appeal. R.S.O. 1970, c. 244, s. 367 (1, 2).

Attorney General to be Heard

- (3) The Attorney General shall be served with notice of any such appeal and is entitled to be heard by counsel upon the hearing thereof. R.S.O. 1970, c. 224, s. 367 (3); 1972, c. 1, s. 9 (7).

Offence

- (4) A rating bureau, insurer or other person failing to comply with such order is guilty of an offence.

Commencement of Section

- (5) This section does not come into force until a day to be named by the Lieutenant Governor by his proclamation. R.S.O. 1970, c. 224, s. 367 (4, 5).

